

**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

In the Matter of	)	
	)	
High-Cost Universal Service	)	WC Docket No. 05-337
Support	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	

**COMMENTS OF GENERAL COMMUNICATION, INC.**

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April 17, 2008

## SUMMARY

Together and individually, the Commission's three Universal Service Fund reform NPRMs propose changes to the High Cost Support systems that are neither "comprehensive" nor "long-term." All three NPRMs undertake "Ready, Fire, Aim" changes without fundamentally defining the objectives and outputs that the Commission and Joint Board seek to achieve through high cost support. Neither the Joint Board nor the Commission propose to define what constitutes "affordable" and "reasonably comparable" rates or "sufficient" support, even though these questions have been pending before the Commission for more than two years and are the subject of a remand from the United States Court of Appeals for the 10<sup>th</sup> Circuit. This akin to driving without a destination – there is no way to know whether you are heading where you want to go. And the Joint Board's proposals and the *Equal Support NPRM* fail to examine 75% of the high cost support that flows to ILECs – focusing solely on the minority of support provided to CETCs.

Poorly defined and executed "reforms" will harm rural consumers and undermine universal service. GCI is currently investing in a transformational, statewide upgrade of Alaska's wireline and wireless networks – reforms that will bring mobile wireless service to nearly 150 small communities that have never had it, that will allow rural consumers automatically to roam statewide and throughout the world, and that will deliver local 1 Mbps broadband to an even greater number of small, rural Alaska communities that have no such service today. But that investment cannot happen without universal service support – the villages GCI will serve are simply too small. And that investment will not happen if the Commission unduly constricts CETC support overall.

GCI understands the need for fiscal sanity in the universal service fund: it supported the adoption of an interim cap on CETC support, with a targeted and limited exclusion for tribal lands to continue to maximize efforts to bring modern services to those traditionally unserved or underserved areas. But true comprehensive and long-term reform must focus on the whole high cost fund, not just the 25% received by CETCs. And it must not cut-off or lock out transformational new investments like GCI's that will bring huge advances in communications capabilities to rural Americans.

As it moves forward, the Commission should take three simple steps to achieve meaningful reform without sacrificing the goals of universal service:

- Continue to support the deployment and operation of innovative and advanced telecommunications on tribal lands – not withdraw support from these areas without specifically examining their needs.
- Limit all ETCs to one support payment per residential/single-line business account – which Qwest estimated would save up to \$500 million per year in CETC support alone.
- Adopt long-proposed numbers-based contribution reform to stabilize the USF contribution mechanism.

On the other hand, the Commission should not:

- Artificially limit the number of ETCs in a given area to one, or to one wireline and one mobile ETC. This would lock out the types of transformational investments that GCI is making, condemning rural America to services that are not comparable to those in urban America. As GCI is demonstrating by its deployment plans, which include entry into 80 Alaska communities of less than 100 lines, the market can best determine when an area can support only one ETC.
- Categorically eliminate CETC support under the ICLS, IAS, and LSS support mechanisms. This would be irrational, discriminatory, and represent a substantial departure from competitively neutral universal service support. In Alaska, nearly 60% of all ILEC support is received through ICLS and LSS; eliminating this support for CETCs would erect formidable barriers to any CETC entering rural Alaska markets.
- Adopt an onerous embedded cost-based USF mechanism for CETCs that would require CETCs to institute Part 32-type accounting systems, with associated cost allocation and affiliate transactions rules. This would drown universal service – and particularly innovative new services offered by CETCs such as GCI – in a sea of unnecessary paperwork.

As the 1996 Act recognized, whether in cars or in telecommunications, competition, not regulation, is the engine that drives rapid innovation and the introduction of the most advanced and useful capabilities. Rural consumers will never have “access to telecommunications and information services, including interexchange services and advanced telecommunications services, that are reasonably comparable to those services provided in urban areas” unless competition – through open market entry – can occur in rural communities. By itself, command-and-control regulation will inevitably bring substantially less innovation and price pressure to rural areas than the market delivers to urban areas. Constraining competition to provide universal service in rural areas condemns rural America to second-class status in communications infrastructure and services.

When Congress was considering the 1996 Act, it expressly recognized that competition and universal service were goals that could and should work together:

Competition and new technologies will greatly reduce the actual cost of providing universal service over time, thus reducing or eliminating the need for universal service support mechanisms as actual costs drop to a level that is at or below the affordable rate for such service in an area.

GCI’s history and plans demonstrates that Congress got it right. The Commission should not now change course and adopt “reform” that limits the ability of the market to bring new, transformational networks and services to rural America.

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**COMMENTS OF GENERAL COMMUNICATION, INC.**

**Introduction**

General Communication, Inc. (“GCI”) hereby comments on the Commission’s three Notices of Proposed Rulemaking, which offer proposals characterized as “long term,” “fundamental,” and “comprehensive” reform of the federal Universal Service high-cost support mechanisms.<sup>1</sup> None of these proposals accomplishes such reform. Real universal service reform is impossible without first defining measureable goals, including the levels of affordable and reasonably comparable rates below which no subsidy would be necessary. These issues, including defining the statutory terms “affordable,” “reasonably comparable,” and “sufficient,” have been pending before the Commission for over two years, yet are not part of these NPRMs. Nor can any proposal

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<sup>1</sup> See *High Cost Universal Service Support*, Notice of Proposed Rulemaking, 23 FCC Rcd 1495, 1508-09 (¶ 35) (2008) (“*Reverse Auction NPRM*”); *High-Cost Universal Service Support*; *Federal-State Joint Board on Universal Service*, Notice of Proposed Rulemaking, 23 FCC Rcd 1467 (2008) (“*Equal Support NPRM*”); *High-Cost Universal Service Support*; *Federal-State Joint Board on Universal Service*, Notice of Proposed Rulemaking, WC Docket No. 05-337 (Rel. Jan. 29, 2008) (“*Recommended Decision NPRM*”) (attaching Recommended Decision, *High-Cost Universal Service Support*; *Federal-State Joint Board on Universal Service*, Recommended Decision, 22 FCC Rcd 20477 (2007) (“*Recommended Decision*”).

that examines only support to CETCs be in any sense “fundamental” or “comprehensive,” as it ignores the *three-fourths* of all support dollars that flow to incumbent LECs. Yet that is what both the Joint Board proposal and the *Equal Support NPRM* do. These two proposals would be little more than another detour on the road to truly comprehensive reform, and thus should be set aside. Reverse auctions may offer the promise of more fundamental reform, but only if properly structured to ensure that market competition will continue to discipline any auction winner.

When conducting any reform effort, the Commission must take care not to throw the universal service baby out with the bathwater. As Congress recognized in enacting the 1996 Act, and as courts have subsequently reaffirmed, competition and universal service work in tandem to the benefit of all consumers. Open entry to rural and high cost areas – which necessarily includes access to universal service support for CETCs – is needed to ensure that the market can drive service improvements and innovations in rural areas just as in urban ones. Only competition can offer “access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas.”<sup>2</sup> Cutting off competition – or raising substantial entry barriers through universal service support mechanisms – will create a permanent digital divide, with urban America receiving advanced services driven by the market, and rural America receiving only the services that regulators mandate or that the monopolist, in its grace, decides to deploy. The nation’s universal service aspirations cannot be fulfilled if the only force driving innovation in rural America is command-and-control regulation.

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<sup>2</sup> 47 U.S.C. § 254(b)(3).



Throughout its history, GCI has demonstrated how competition can fulfill the fundamental goals of universal service. In the long distance market, GCI was the first carrier to eliminate “double-hopped” satellite transmissions between communities in the Alaska bush. GCI’s entry into local markets forced the ILEC to introduce services such as fractional T-1s and digital switching services that was previously unavailable in Alaska. And now GCI is in the process of building out the first statewide wireless network, which will bring modern digital wireless service with statewide roaming and broadband services at speeds, ultimately, of 1 Mbps or more to not just Alaska’s urban and regional centers, but also to some 90,000 Alaska residents that live in tiny communities outside of those areas. Even in the urban areas that have multiple ETCs today, no carrier has yet deployed a network that will allow consumers to roam anywhere in Alaska. GCI’s new network will be the first, unless the Commission radically alters the available universal service support. GCI is demonstrating the power of competition to drive both the preservation and the *advancement* of universal service, consistent with Section 254(b). Moreover, by deploying alternative facilities-based networks, GCI will improve not only consumer choice, but also public safety by providing an alternative to the ILEC’s network. Yet GCI’s ability to deliver these tremendous universal service benefits – bringing 90,000 Alaskans outside of the urban and regional centers access basic and advanced telecommunications services truly comparable to those available in the lower 48 – is dependent on GCI’s continued ability to obtain universal service support for the customers that it serves.<sup>3</sup>

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<sup>3</sup> Competitively neutral access to universal service support is also critical to GCI’s ability to expand and continue to provide competitive wireline services.

None of the NPRMs before the Commission can satisfactorily ensure that ETCs – individually or collectively – will continue to upgrade their networks and deploy innovative new services in the rural and high cost areas that receive universal service support. None of the NPRMs proposes universal service mechanisms that harness the invisible hand of marketplace competition to drive innovation and service improvements in supported services, just as we rely on that hand throughout the rest of our economy. Instead, each of the proposals will necessitate a return to command-and-control regulation, which can never be as effective as the market in stimulating service innovations and network upgrades.

The Joint Board’s Provider of Last Resort (“POLR”) Fund contemplates supporting only ILEC networks, raising a huge barrier to entry for any other service provider. The same is true for eliminating CETC access to ICLS and LSS support, as proposed in the *Equal Support NPRM*. The Commission’s reverse auction proposal would similarly result in a single universal service recipient for some term of years. When there is only one support recipient – whether selected through auctions, by the regulator, or by limiting support to POLRs – there is no ongoing incentive to upgrade vigorously networks and services. The “own costs” support proposed in the *Equal Support NPRM* would likewise reject the market by providing greater support to higher-cost carriers than to lower cost carriers when both are competing to provide the same services to the same customer in the same place, eliminating the usual marketplace reward for increased efficiency. Finally, the “own costs” proposal contemplates the

extension of rate-of-return regulatory structures and mechanisms to CETCs – a far cry from the 1996 Act’s “pro-competitive, deregulatory national policy framework.”<sup>4</sup>

That is not to say that there are not reforms that could be made quickly pending a truly comprehensive review and reform of the entire high-cost mechanism, including high-cost ILEC support. For example, as the Joint Board has suggested, the Commission could adopt an interim cap on CETC support, but with a tribal lands exclusion as GCI has previously proposed. Likewise, it could extend the proposed interim caps to all ETCs – not just CETCs – in all locations where a CETC offers service, again subject to a tribal lands exclusion. That would at least bring greater discipline to both ILEC and CETC payments instead of ignoring the 75% of the fund that is comprised of ILEC support. In addition, to the extent that the Commission is concerned about support mushrooming because of wireless “family plans,” the Commission could limit high cost USF support for CETCs to one payment per residential or single-line business account, rather than paying an equivalent support amount for each handset in the wireless “family plan.” Qwest has estimated that such a limitation would reduce high cost support by as much as \$500 million per year. Unlike many of the proposals in the NPRMs, this simple reform could be implemented in the near term and, thus, it has the potential to reduce the strain on the fund almost immediately. Finally, the Commission could address concerns about the increasing level of its contribution factor by resolving its long-standing contribution reform proceeding and adopting a numbers-based contribution system.

The Commission should also not adopt the Joint Board’s proposal to create a separate “mobility” fund that limits support to a single wireless provider and to capital

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<sup>4</sup> S. Rep. No. 104-23, at 1 (1995).

spending for new construction. This proposal is backward-looking, ignores the fact that the most capable and cost-effective networks now and in the future for rural areas may be wireless, and is unlikely to provide sufficient support in hard-to-serve areas such as the small communities in the Alaska bush – many of which have far fewer than 100 lines. In these small communities, there is simply not going to be a large enough subscriber base – even at 100 % subscription – to cover operational costs once the network is deployed.

Irrespective of whether the Commission adopts any of the so-called “long term” reform alternatives, the Commission should not now begin to withdraw or otherwise compromise support for tribal lands. As the Commission has long recognized, even basic telephone subscribership on tribal lands lags far behind the rest of the country. Moreover, these areas are the most in need of advanced telecommunications infrastructure to promote economic development. Furthermore, they are but a tiny part of the overall telecommunications markets in the country – and a tiny portion of the consumers for whom carriers receive universal service support. The Commission should simply exempt tribal lands from any changes (save for those adopted as part of any tribal lands exemption in the interim cap proceedings) pending further review in a proceeding specific to tribal lands. Preservation of support for tribal lands, along with fund-wide, per-account based controls and contribution reform, are core components of any sustainable long-term reform package.

These comments proceed in three parts.<sup>5</sup> Part A begins by revisiting the principles underlying universal service and explains the continued need for competitors

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<sup>5</sup> The Comments are divided into three Parts for the convenience of the reader. The Comments as a whole, however, respond to each of the three NPRMs and are expressly incorporated into the record in response to each NPRM.

like GCI to ensure these principles are fulfilled. Part A also addresses the overboard proposals offered in the *Joint Board NPRM*, responds to the many failings shared by two or more of the proposals advanced in the Commission's three NPRMs, and details the particular harms that would arise if CETCs were discriminatorily denied ICLS and LSS support. Part B responds in particular to other proposals contained in the *Equal Support NPRM*. Part C responds in particular to other proposals contained in the *Reverse Auctions NPRM*.

## **PART A – GENERAL PRINCIPLES AND COMMON CONCERNS**

### **I. CETCs Are Critical to Ensuring that Rural America Receives Services Comparable to Urban America at Affordable Rates.**

GCI's past experience and future plans demonstrate how CETCs play a critical role in delivering modern communications services to rural America and fulfilling the Act's universal service goals. Indeed, GCI's story shines as an example of the power of competition, as opposed to command-and-control regulation, to bring advanced and modern telecommunications services to even the most remote areas of the nation. GCI distinguishes itself from its competitors by offering its customers lower prices, more choices, and better service, even in remote communities in Alaska with populations under a few hundred – far below the threshold often assumed necessary for competition. As described in previous comments filed with the Joint Board and the Commission, GCI's entry into markets throughout Alaska has forced its competitors to improve and expand their own offerings, benefiting consumers statewide.<sup>6</sup>

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<sup>6</sup> See *Federal-State Joint Board on Universal Service; The Merits of Using Auctions to Determine High-Cost Universal Service Support*, Comments of General Communication, Inc., WC Docket No. 05-337 (filed Oct. 10, 2006) ("GCI Reverse Auction Comments"); *Federal-State Joint Board on Universal Service; High-Cost*

GCI's entry into the Alaska communications markets revolutionized long distance services. By employing then state-of-the-art DAMA satellite technology, GCI eliminated the "two-hop" transmission of telephone calls, which for the first time allowed Alaska's rural bush communities to connect calls both to other bush communities and to the lower 48 states without the latency and low quality that two-hopping created. With two hopping, even sending a fax was a complex and rarely successful undertaking. When GCI entered local telephone markets, it similarly improved service offerings and quality. GCI was the first company to offer digital subscriber services for businesses, as well as ISDN PRI service, in Fairbanks and Juneau. GCI led the way in introducing fractional T-1s. GCI pioneered night installations for businesses, which incumbent ACS had previously refused to perform. GCI introduced consumer-friendly packages of local service plus custom calling features and prices that were substantially below the ILEC's price before competition. In Alaska, GCI in the marketplace has proved the Commission's assessment that "designation of qualified ETCs promotes competition and benefits consumers by increasing customer choice, innovative services, and new technologies."<sup>7</sup> Imbalanced USF policies, however, would have tipped the scales against

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*Universal Service Support*, Comments of General Communication, Inc., CC Docket No. 96-45 and WC Docket No. 05-337 (filed Mar. 27, 2006) ("*GCI Qwest II Remand Comments*"); See *Federal-State Joint Board on Universal Service; High-Cost Universal Service Support*, Reply Comments of General Communication, Inc., CC Docket No. 96-45 and WC Docket No. 05-337 (filed May 26, 2006); *Comprehensive Review of Universal Service Fund Management, Administration, and Oversight*, *Federal-State Joint Board on Universal Service*; Comments of General Communication, Inc., WC Docket No. 05-195 and CC Docket No. 96-45 (filed Oct. 18, 2005).

<sup>7</sup> *Federal State Joint Board on Universal Service; RCC Holdings, Inc. Petition for Designation as an Eligible Telecommunications Carrier Throughout its Licensed Service Area In the State of Alabama*, Memorandum Opinion and Order, 17 FCC Rcd 23532, 23540-41 (¶ 23) (2002); see also *Federal-State Joint Board on Universal*

GCI in the market, undoubtedly limiting its abilities to compete fully and deliver these consumer benefits.

Competition continues to fuel expanded services for Alaska consumers. GCI is in the midst of rolling out a local service platform that will deliver statewide fixed and mobile wireless services and advanced Internet service. In the urban areas of Alaska (Anchorage, Fairbanks, Juneau, and their suburbs, such as the Matanuska Valley) and in many of the regional centers, GCI is upgrading its cable plant and will provide telephone service predominantly over its own cable facilities, supplemented by resold services where necessary. GCI will also offer mobile services in these areas over its own facilities.

Unless the Commission significantly alters the available universal service support, GCI is planning to invest more than \$200 million over the next three years to upgrade its cable systems and deploy mobile wireless and high-speed Internet service in remote areas outside of the Alaskan road system integrating cable, satellite, and wireless technologies.<sup>8</sup> GCI's plan will revolutionize wireline and wireless communications services throughout the state, including bringing mobile wireless service to 90,000 Alaskans, most of whom live in villages that lack mobile wireless service today, and upgraded wireless capability

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*Service; Western Wireless Corporation Petition for Designation as an Eligible Telecommunications Carrier for the Pine Ridge Reservation in South Dakota, Memorandum Opinion and Order, 16 FCC Rcd 18133, 18137 (¶ 12) (2001).*

<sup>8</sup> Transcript, Special Public Meeting, Regulatory Commission of Alaska (Dec. 11, 2007) ("RCA Transcript") *available at* <https://rca.alaska.gov/RCAWeb/ViewFile.aspx?id=c5b93bad-8e67-4620-ae8d-7a0e23ce32fc>. GCI will also offer wireline local service, via resale, for rural customers that request such service. GCI cannot, however, provide advanced broadband capability or the benefits of a diverse, facilities-based network via resale.

to an additional 50,000 Alaskans in regional centers and other places that currently enjoy only limited wireless capability today.<sup>9</sup>

When GCI's statewide rollout (including the wireless component) is complete, GCI will have deployed advanced mobile voice and broadband service in over 185 rural Alaska communities – 145 of which are under 200 total lines and at least 80 of which are under 100 lines. The vast majority of these communities would have mobile wireless service for the first time, and would have Internet access of approximately 1 Mbps (local connectivity) for the first time. Even among the communities that currently have some form of wireless service, GCI's rural deployment would allow consumers to roam automatically to Alaska's urban centers and to the rest of the United States and the world, which few can do today.<sup>10</sup>

The map below dramatically depicts the transformational nature of GCI's rural wireless and other statewide deployments. Figure 1 contrasts the limited number of communities with wireless mobile voice service in Alaska today with the numerous Alaskan communities currently lacking mobile voice service that will have access to such service after GCI's rural wireless deployment is complete. Each red dot on the map below represents a community without wireless today that will have wireless when GCI's deployment is complete. With this deployment, for the first time, consumers will be able to roam among villages and regions seamlessly, and mobile subscribers from the rest of the country and the world will be able to roam throughout Alaska.

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<sup>9</sup> RCA Transcript at 9-10.

<sup>10</sup> *Id.* at 10.





year, improved mobile access to public safety will be particularly valuable. Moreover, because GCI is deploying local switches in all areas with satellite backhaul, these rural Alaskans will not have to worry that they will lose access to local emergency services if their satellite services are disrupted.

In addition, GCI's planned rural deployment will put in place another network, which, as the aftermath of Hurricane Katrina showed, can be critical if the ILEC network fails. The Regulatory Commission of Alaska ("RCA") recently opened an investigation into multi-day (sometimes multi-week) outages that have been plaguing the southeastern Alaskan communities of Thorne Bay and Klawock, where ACS is the incumbent LEC.<sup>11</sup> As ACS has told the RCA in connection with the Thorne Bay and Klawock outages, when those customers lose dial-tone, they cannot place 911 calls.<sup>12</sup> If these problems had occurred after GCI had already launched its planned rural wireless service in those communities, both consumers and public safety would have had an alternative network available.

The transformational nature of GCI's rural wireless and other statewide wireless deployments (not to mention prior and planned wireline deployments and upgrades) are even more dramatic with respect to the availability of broadband at 1 Mbps or greater.

Figure 2 shows the availability of 1 Mbps broadband service today. Figure 3 shows the

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<sup>11</sup> See *The Investigation of Local Exchange Service provided by ACS OF THE NORTHLAND, INC. d/b/a ALASKA COMMUNICATIONS SYSTEMS, ACS LOCAL SERVICE and ACS in Thorne Bay and Klawock, Alaska*, RCA Order Opening Investigation, Inviting Participation, Inviting Intervention, Requiring Filing, Addressing Timeline for Decision, Designating Commission Panel, and Appointing Administrative Law Judge, Order No. 1, RCA Docket No. U-08-23 (Feb. 15, 2008).

<sup>12</sup> *The Investigation of Local Exchange Service provided by ACS OF THE NORTHLAND, INC. d/b/a ALASKA COMMUNICATIONS SYSTEMS, ACS LOCAL SERVICE and ACS in Thorne Bay and Klawock, Alaska*, ACS-N Response, RCA Docket No. U-08-023 (filed March 14, 2008).

tremendous increase in that availability after GCI's rural wireless deployment is complete. And because GCI is using software-defined radios, these broadband speeds will be more easily upgradable as technology advances.



**Figure 2: Local and Rural 1 Mbps Broadband Today<sup>13</sup>**

<sup>13</sup> Figure 2 identifies those communities that currently have (or likely have) access to DSL or cable modem service at estimated speeds of 1 Mbps or more. Not surprisingly, these communities tend to be in and around urban areas. The underlying data was taken directly from the Regulatory Commission of Alaska (“RCA”), *see* RCA Internet Connectivity Spreadsheet (Jan. 12, 2007) *available at* [http://www.state.ak.us/rca/Broadband/Internet\\_connectivity-070112.pdf](http://www.state.ak.us/rca/Broadband/Internet_connectivity-070112.pdf), and supplemented with publicly available information from other carriers for communities where the RCA data was inconclusive and to determine the advertised speeds of LEC DSL services. ATA has quibbled with what it saw as a few omissions

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in previous versions of similar maps. *See High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Alaska Telephone Association Ex Parte Letter, WC Docket No. 05-337 and CC Docket No. 96-45, at 1 (filed Mar. 21, 2008). While GCI has been diligent in presenting what it believes to be the best information available, it has undertaken to review the community listings using the limited information that is available on this topic, revising the map, and clarifying what it depicts accordingly. This depiction, in fact, is probably over-inclusive, because it contains all DSL-served communities where advertised offerings included speeds of 1 mbps or more, even where such services were only offered to residential customers, or when availability specifications on a per-community basis were unavailable. These revisions only reinforce the point – LEC service offerings remain tightly bound to the road-served, urban areas of the state, with rural areas relegated to little better than dial-up speeds – as even ATA’s own filing confirms. While ATA seems content to offer unhelpful sniping that fails to further USF reform, the fact is that GCI’s rural deployment will greatly increase the access to broadband services well beyond DSL-levels (up to 1 Mbps) in rural areas that are currently underserved.



**Figure 3: Local and Rural 1 Mbps Broadband After GCI Rollout<sup>14</sup>**

<sup>14</sup> Figure 3 depicts the availability of 1 Mbps broadband service following GCI's rollout of its new rural wireless network – assuming that deployment proceeds and is not interrupted by changes in the universal service regime for high cost areas. GCI's broadband cable modem service offers multimegabit broadband service to approximately 80 percent of Alaskan homes, located predominantly in Alaska's urban, suburban and regional centers. In more remote areas, GCI will offer high-speed Internet service using broadband platforms that integrate cable, satellite, and wireless technologies. GCI's current 256 kbps wireless systems are in need of upgrades, both to provide higher speeds and to achieve full CALEA functionalities for traffic traveling solely within a particular WISP or DSL node. In both Figures 2

There is no doubt that these rural communities desire the same types of communications services as are available in the rest of the country. Rural Alaskans want to be able to use cell phones, PDAs, and the Internet in the same way that the rest of Alaska and the country can. As an example, GCI currently offers high-speed wireless Internet services of up to 256 kbps at affordable prices to 127 villages and serves 20 more villages by partnering with other providers and using wireless or DSL. To take just two examples, even at these comparatively low speeds, by urban standards, GCI provides Internet service to more than 50 percent of the households in Akutan, a village located on Akutan Island in the eastern Aleutians with a population of 713, and to 91 percent of the 32 households in the tiny village of Atka, population 92.

GCI's rural wireless deployment will also provide a long-term engine for continued innovation and enhancement of universal service in these remote rural communities. In all areas, GCI will offer services that fully substitute for – not merely complement – those available from the ILEC. Accordingly, GCI's deployment will bring vigorous competition for customers between GCI and the incumbent LEC, which in turn will provide a market-based mechanism to ensure that rural Alaska receives access to the same advanced telecommunications services that are available in Alaska's urban centers and in the lower 48 states. Both GCI and its competitors will have to continually work to upgrade their services to provide the most modern capabilities to rural Alaskans.

This will be a far superior means for spurring continued innovation than command-and-control regulation. The impending threat of GCI's market entry has produced positive competitive effects in remote areas of Alaska where GCI has been

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and 3, where GCI provides cable modem service, the ILEC also typically provides DSL service.

authorized to provide service. In Nome, for example, where GCI acquired existing cable plant and began offering high-speed Internet access through cable modems, the Mukluk Telephone Company started offering its own high-speed Internet service.<sup>15</sup> The Matanuska Telephone Association and the Ketchikan Public Utility have likewise responded to GCI's anticipated market entry in their service areas by upgrading their traditional telecommunications networks to provide video services.<sup>16</sup> So, too, in Barrow, the Arctic Slope Telephone Association Cooperative began offering its own high-speed Internet service only after GCI acquired an existing cable system and offered high-speed, cable modem Internet access. And GCI's prospective entry into remote villages has also stimulated TelAlaska's efforts to initiate its own wireless offering. The Alaskan experience provides strong evidence that the competitive process, not regulatory fiat, is the best means to ensure delivery of universal service at minimum cost to all consumers, even in small rural communities.

However, GCI will be unable to make this transformational network investment – and none of these tremendous public interest benefits will come to fruition – if there are dramatic changes in the universal service support available to GCI as a CETC. For example, the economics of a 25-person or 25-home village (or even a 200-home community) simply do not allow for such investment on a stand-alone basis. At best,

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<sup>15</sup> GCI's local service certificate was amended to include Nome on February 6, 2006. *The Application by GCI COMMUNICATION CORP. d/b/a GENERAL COMMUNICATION, INC. and GCI for an Amendment to its Certificate of Public Convenience and Necessity to Operate as a Competitive Local Exchange Telecommunications Carrier, Order Approving Remaining Portions of Application Subject to Conditions, Addressing Service Area Issues, and Requiring Filings, Order 6, RCA Docket No. U-05-046 (Feb. 2, 2006).*

<sup>16</sup> These upgrades have been supported by federal USF support because the ILECs upgrade the loop plant in their regulated utility subsidiary, then sell that transmission capacity to their unregulated video affiliates.



GCI estimates that the revenue from subscribers for these services can cover approximately half of the costs of deploying and operating its rural wireless network.<sup>17</sup> But GCI is not asking to receive support for the costs of deploying its network irrespective of the number of customers served – as the ILECs currently do – and thus GCI will need far less aggregate support than the ILEC currently receives to provide far greater capability. GCI believes the economics of deploying these services, even to these very small villages, will work with CETC support roughly comparable to the ILEC's on a per line basis – even when limited to one support payment for a residential or single-line business account.<sup>18</sup> This is essentially what the USF interim cap with the tribal lands exclusion would permit, and why the tribal lands exclusion is critical to allowing GCI to proceed with its transformational investment.

GCI's planned rural network expansion also illustrates the need for universal service policies that accommodate the development and deployment of new, cost-efficient technologies, and the very real potential for limits on the number of supported CETCs to lock new, more capable and efficient technologies out of the market. Approximately five years ago, GCI set out to develop a solution that could bring robust wireless service to areas in rural Alaska not on the road network at a cost that would be economically feasible. Among the business and technical challenges was finding a full wireless system that could be deployed for under \$100,000 per village – but with local switching that could be deployed in the villages themselves so that intra-village calls

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<sup>17</sup> RCA Transcript 11-13.

<sup>18</sup> *Id.* at 59.



would not have to be “double-hopped” via satellite to Anchorage.<sup>19</sup> This equipment also had to be capable of being barged or airlifted in, and installed with hand tools.

Five years ago, the technology had not yet developed to the point that GCI’s rural wireless project was possible. Now, it has. GCI worked diligently in the intervening years not only to develop and employ efficient and innovative methods of field construction and system implementation, but also to drive equipment vendors to produce wireless products that utilize new technologies. Integrating such technologies as IP soft-switching and software-defined radios, GCI now will be able to deploy a robust system that is economically feasible and that will provide a readily upgradeable path for faster broadband services as both local network and backbone technology advance.

If the Commission had, before now, limited the number of supported ETCs in any study area to one, it would have locked GCI out of the rural market entirely. A single winner auction would have had the same effect. GCI could not have bid because the technology to permit a commercially feasible deployment had not yet become commercially available. Consumers would have been denied the opportunity to benefit from this deployment, as, even now, no other carrier or group of carriers is seeking to roll out these services in these off-road areas on a statewide basis. Open market entry remains a cornerstone for permitting the market to drive service advances and innovations whenever technological change makes it economically feasible to do so.

GCI is certainly proud of its efforts to bring new technologies to rural Alaska, but the company tells its story here not as an exercise in self-promotion, but rather in an effort to explain that USF *must* allow and, indeed, encourage the kind of innovation and

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<sup>19</sup> *Id.* at 11.

expansion upon which GCI has embarked. Competition among ETCs in rural areas inevitably forces carriers to improve their own service quality, benefitting both consumers and public safety. GCI's deployment is at the core of what universal service is, and what it should be, about. Any reform that would stunt this sort of innovation, by limiting technologies or competition, will harm the underserved communities that the universal service fund was designed to help.

## **II. Universal Service Support in Tribal Lands Must not be Compromised.**

Because even basic telephone subscribership on tribal lands lags far behind levels in the rest of the country,<sup>20</sup> the Commission has expressly recognized the need for “Commission action to promote the deployment of telecommunications facilities in tribal areas and to provide the support necessary to increase subscribership in these areas.”<sup>21</sup> Closing this gap on tribal lands is necessary to fulfill the Congressional mandate that consumers “in all regions of the Nation, including low-income consumers and those in rural, insular, and high-cost areas. . . . have access to telecommunications and information services.”<sup>22</sup> Adopting any “reform” that abandons this goal by reducing funding in tribal areas would leave residents of tribal lands with little hope of catching up

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<sup>20</sup> See *Federal-State Joint Board on Universal Service; Promoting Deployment and Subscribership in Unserved and Underserved Areas, Including Tribal and Insular Areas*, Twelfth Report and Order, Memorandum Opinion and Order, and Further Notice of Proposed Rulemaking, 15 FCC Rcd 12208, 12211-12 (¶ 5) (2000) (noting that, based on then-available data, “only 47 percent of Indian tribal households on reservations and other tribal lands have a telephone”).

<sup>21</sup> See *id.*, 15 FCC Rcd at 12213 ¶ 5; see also *Extending Wireless Telecommunications Services to Tribal Lands*, Report and Order and Further Notice of Proposed Rulemaking, 15 FCC Rcd 11794 (2000) (establishing tribal lands bidding credits).

<sup>22</sup> 47 U.S.C. § 254.

with the rest of America. That outcome would be unfair and, because it directly contradicts the principles underlying universal service, unlawful.

The record in this proceeding and others already demonstrates the need for – at a minimum – undiminished support for tribal areas.<sup>23</sup> While scant, the current data on availability of telecommunications services in tribal lands shows that any reduction in support would be woefully premature. The GAO notes that “telephone subscribership rate for Native Americans living on tribal lands has historically lagged behind the overall national rate.”<sup>24</sup> The most recent data available shows that only 68.6 percent of Native American households on tribal lands in the lower 48 states subscribe to telephone service, “substantially below the national rate of 97.6 percent.”<sup>25</sup> When three households in ten do not have telephone service, service is hardly universal. And a nearly 30-point gap in subscribership levels hardly evidences reasonably comparable service in tribal lands and elsewhere in America. These gaps may never close if efforts at broader reform curtail existing support for tribal lands.

While virtually no data is available, there is no evidence that wireless and advanced telecommunications subscribership rates on tribal lands are any better. The GAO has found that “the rate of Internet subscribership is unknown because no federal

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<sup>23</sup> See *Federal-State Joint Board on Universal Service, High Cost Universal Service Support*, GCI Ex Parte Letter, CC Docket 96-45 (filed May 31, 2007) (“GCI Long Term Reform Ex Parte”); see also *Federal-State Joint Board on Universal Service, High Cost Universal Service Support*, Alaska Federation of Natives, Inc. Ex Parte Letter, WC Docket No. 05-337 and CC Docket No. 96-45, at 1 (filed June 11, 2007) (“Alaska Federation of Natives Letter”).

<sup>24</sup> *Challenges to Assessing and Improving Telecommunications for Native Americans on Tribal Lands*, at 1, United States Government Accountability Office, Report to Congressional Requesters, Jan. 2006, GAO-06-189 (“GAO Report”).

<sup>25</sup> *Id.* at 10.

survey has been designed to capture this information for tribal lands.”<sup>26</sup> The National Tribal Telecommunications Association notes that the Commission’s reports on CMRS competition “have specified very little, if any, data particular to communications services on tribal lands.”<sup>27</sup> It is clear, however, that availability of both basic and advanced telecommunications services is critical to tribal lands, as “Native American tribes are among the most economically distressed groups in the United States.”<sup>28</sup> Providing access to advanced telecommunications services is critical to ensure that residents of tribal lands are not “denied the economic, educational, public health, and public safety benefits that Congress intended the [Universal Service] Fund to provide.”<sup>29</sup> The Commission cannot abandon the effort to bring advanced services to tribal lands before it even understands what services are (and are not) available today. The available evidence strongly suggests that continued support is needed to keep these chronically underserved areas from falling further behind.

Any reform that overlooks the heightened need for universal service support on tribal lands will, in effect, sacrifice fundamental universal service goals in the name of preserving universal service. Instead, the Commission should continue its commitment to universal service, and its established precedent of taking steps specifically responsive to the needs of tribal lands, by ensuring that any reforms it adopts preserve existing support for tribal lands.

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<sup>26</sup> *Id.*

<sup>27</sup> *See Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; Annual Report and Analysis of Competitive Market Competition with respect to Commercial Mobile Services*, Comments of the National Tribal Telecommunications Association, WT Docket Nos. 07-71 and 08-27, at 2 (filed Mar. 26, 2008).

<sup>28</sup> GAO Report at 9.

<sup>29</sup> *See Alaska Federation of Natives Letter* at 1.

**III. None of the Proposals in the Three NPRMs Achieves Competitively Neutral or Fundamental USF Reform.**

**A. None of the NPRMs Proposes Defining The Measurable Outputs High Cost Universal Service Support is Supposed to Achieve For Consumers in the Market.**

Despite claiming to undertake “fundamental” and “comprehensive” high-cost distribution reform,<sup>30</sup> the three NPRMs propose reforms that are neither fundamental nor comprehensive. Most troubling, the Joint Board recommendations and the *Equal Support NPRM* propose mechanisms designed to cut support for CETCs without proposing similar reforms to reduce ILEC support – which totals three-fourths of all high-cost support. Moreover, no reform can be fundamental or comprehensive without identifying the measureable objectives of high cost universal service support. Indeed, without confronting this issue, any changes will be nothing more than interim “Ready, Fire, Aim” short-term measures destined to bring us no closer to real reform.

This failure to tackle these serious, foundational issues is well-known and well-documented. In 2005, the U.S. Office of Management and Budget (“OMB”) found that the high-cost fund “lacks measures and goals to assess performance” and, further, that “the program does not measure the impact of funds on telephone subscribership in rural areas or other potential measures of program success, nor does it base funding decisions on measureable benefits.”<sup>31</sup> The Commission has also recognized that “effective program management requires the implementation of *meaningful performance measures*”

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<sup>30</sup> See, e.g., *Recommended Decision*, 22 FCC Rcd at 20478 ¶ 1; *Equal Support NPRM*, 23 FCC Rcd at 1470 ¶ 5; *Recommended Decision NPRM* at ¶ 7 (seeking “comment on specific high-cost universal service *comprehensive* reform proposals”) (emphasis added).

<sup>31</sup> Office of Management and Budget, Universal Service Fund High Cost Program Assessment, 2005, <http://www.whitehouse.gov/omb/expectmore/summary/10004451.2005.html>.

and that “[c]learly articulated goals and reliable performance data allow the Commission and other stakeholders to assess the effectiveness of the USF programs and to determine whether changes are needed.”<sup>32</sup> Almost three years later, however, the Commission has failed to implement that policy.

Even worse, the *Recommended Decision* reverses course from the Commission’s commitment in the *USF Management NPRM* to develop performance measurements based on outputs and outcomes. The *Recommended Decision* fails even to acknowledge this commitment and instead proposes to maintain the existing support for ILECs, which focuses on carriers’ inputs (*i.e.*, costs) without any examination of outputs (*i.e.*, price and subscribership).<sup>33</sup> As Congress has recognized, defining outputs and outcomes for federal programs is essential to proper management and oversight, and to preventing waste, fraud, and abuse.<sup>34</sup> With the high cost universal service program, the need for

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<sup>32</sup> *Comprehensive Review of Universal Service Fund Management, Administration, and Oversight; Federal-State Joint Board on Universal Service; Schools and Libraries Universal Service Support Mechanism; Rural Health Care Support Mechanism; Lifeline and Link-Up; Changes to the Board of Directors for the National Exchange Carrier Association, Inc.*, Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, 20 FCC Rcd 11308, 11318-19 (¶ 24) (2005) (“*USF Management NPRM*”) (emphasis added).

<sup>33</sup> *Recommended Decision NPRM* at ¶¶ 19-23.

<sup>34</sup> See, e.g., Government Performance and Results Act of 1993, Pub. L. No. 103-62, § 2, 107 Stat. 285 (codified in scattered sections of 31 U.S.C.) (finding that “(1) waste and inefficiency in Federal programs undermine the confidence of the American people in the Government and reduces the Federal Government’s ability to address adequately vital public needs; (2) Federal managers are seriously disadvantaged in their efforts to improve program efficiency and effectiveness, because of insufficient articulation of program goals and inadequate information on program performance; and (3) congressional policymaking, spending decisions and program oversight are seriously handicapped by insufficient attention to program performance and results”); see also D. Osborne & T. Gaebler, *Reinventing Government: How the Entrepreneurial Spirit is Transforming the Public Sector* 139 (Plume 1993) (“Traditional bureaucratic governments . . . focus on inputs, not outcomes. . . . They pay little attention to outcomes – to *results*.”).

performance measures is especially acute. Now is the time for the Joint Board and the Commission to cure this fundamental shortcoming. Any reform that fails to address these issues cannot fairly be called “fundamental,” “comprehensive,” or “long-term.”

Furthermore, although the Commission sought comment on the issue over two years ago in this very docket in response to a judicial remand, it never defined the key statutory terms “reasonably comparable” and “sufficient,” nor has it defined “affordable.”<sup>35</sup> As GCI pointed out at the time<sup>36</sup> and as others continue to acknowledge today, the Commission must define these terms and define them based on the specific outputs of subscribership and rate levels sought in the marketplace. In response to these three NPRMs, members of the Mercatus Center at George Mason University, for example, conclude that “[t]o know whether universal service programs have or are likely to provide access to reasonably comparable services at reasonable rates, the FCC must first define and measure what counts as availability of service and ‘reasonably comparable’ rates.”<sup>37</sup> Without defining these fundamental terms – and defining them with respect to the class of consumers who are *not* eligible for Lifeline support – the Commission has skipped over a necessary predicate to real reform.

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<sup>35</sup> *Federal-State Joint Board on Universal Service; High-Cost Universal Service Support*, Notice of Proposed Rulemaking, 20 FCC Rcd 19731 (2005) (“*Tenth Circuit Remand II NPRM*”).

<sup>36</sup> *GCI Qwest II Remand Comments*; GCI Long Term Reform Ex Parte; *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service*, GCI Comments, WC Docket No. 05-337 and CC Docket No. 96-45 (filed Sept. 30, 2005).

<sup>37</sup> *See High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Comments of the Mercatus Center at George Mason University, WC Docket No. 05-337 and CC Docket No. 96-45, at 3 (filed Mar. 27, 2008) (“*Mercatus Center Comments*”).

As an initial matter, any attempt at truly fundamental and comprehensive reform must answer certain key questions:

- What supported service must an ETC provide?
- At what price?
- Over what area?
- Subject to what terms and conditions?

Failure to grapple with and ultimately resolve these admittedly complex issues will undermine any attempt at “fundamental” universal service reform. Most notably, failure to answer these questions would convert any reverse auction into a “comparative hearing”-type process in which the Commission is subjectively weighing multiple factors. As the Commission and Congress learned long ago in the spectrum context, comparative proceedings are slow, inefficient, and prone to politically-driven decision making. This is, of course, why Congress enacted spectrum auctions in the first place.

Because defining performance measures is necessary to sensible reform, the Commission cannot proceed as if such measures are mere afterthoughts. Otherwise, the Joint Board and the Commission are engaging in a rudderless process that cannot provide a clear way to determine whether specific reform measures improve universal service or cost effectiveness. To the Commission’s credit, the *Reverse Auction NPRM* at least raises some of these questions, seeking comment, for example, about mandatory broadband speeds and how to ensure that broadband is offered at “reasonable prices.”<sup>38</sup> But, the *Reverse Auction NPRM* does not define the crucial parameters of service and

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<sup>38</sup> See *High Cost Universal Service Support*, Notice of Proposed Rulemaking, 23 FCC Rcd 1495, 1508-09 (¶ 35) (2008) (“*Reverse Auction NPRM*”).



retail price with respect to the core voice services.<sup>39</sup> It is difficult to see how the Commission could set a reserve price and conduct an auction to determine the amount of support to be provided without first telling the bidders how much revenue they will be allowed to collect from consumers for the basic supported service. Moreover, without answering these questions, the Commission will be unable to assure itself that the auction will result in support “sufficient” to achieve “affordable” and “reasonably comparable” universal service rates and, thus, fulfills Section 254’s objectives.

Fortunately, the Commission can answer these questions without delay, as the Commission has already sought and received comment on performance measures for the high-cost program in the *USF Management NPRM* and the *Tenth Circuit Remand II NPRM*.<sup>40</sup> As part of its consideration of long-term reform, the Commission should incorporate the record from those proceedings here and rely on those comments to define, once and for all, the outputs that are sought from high-cost universal service support mechanisms.

To be effective, outcome/output measures must be based on functionality and not tied to specific technologies or regulatory classifications. For example, the Joint Board’s proposal to create a three-fund system for “broadband” providers, “mobility” providers, and POLRs begs the question of what specific outcomes these funds are designed to achieve – and how their proposed structures and eligibility limitations are tied to those outcomes. Chairman Martin understands that “[t]he communications industry is going through a time of unprecedented change,” recently stating, “[i]t is difficult to envision

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<sup>39</sup> See *id.*, 23 FCC Rcd at 1504-09 ¶¶ 23-35.

<sup>40</sup> *USF Management NPRM*, 20 FCC Rcd at 11308; *Tenth Circuit Remand II NPRM*, 20 FCC Rcd 19731.

how the communications landscape will look in 15, 10, or even five years from now.”<sup>41</sup>

In that light, it makes no sense to hamstring potential providers of universal service by providing technology-specific support.

GCI’s scheduled deployment illustrates the wisdom of a technology-neutral approach. GCI plans to incorporate satellite, wireline, and wireless technologies to provide consumers in rural Alaska with residential and mobile voice service, as well as broadband service. From the customer’s – and the statute’s – perspective, the underlying technology is irrelevant, so long as the customer receives reliable, affordable service. (Indeed, some ILECs have for years offered their supported universal service through wireless services – often labeled as basic exchange telephone radio service (“BETRS”).) Accordingly, the Commission should define the high-cost fund objectives in terms of what consumers, rather than carriers, receive. Focusing on inputs, as the current and proposed high-cost system does, incorrectly makes carriers, rather than consumers, the beneficiaries of universal service support.<sup>42</sup>

Furthermore, the Joint Board and the Commission must explicitly identify in objective, measurable terms any additional factors to be considered in setting levels of ETC support or selecting ETC providers. For example, the Joint Board and the Commission should specify any minimum quality of service requirements or

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<sup>41</sup> Kevin J. Martin, FCC Chairman, Remarks at CTIA Wireless 2000, at 1 (Apr. 1, 2008) (“Chairman Martin’s CTIA Remarks”).

<sup>42</sup> *Alenco Communs., Inc. v. FCC*, 201 F.3d 608, 620 (5th Cir. 2000) (stating that the Act is not meant to “guarantee all local telephone service providers a sufficient return on investment; quite to the contrary, it is intended to introduce competition into the market. . . . The Act only promises universal service, and that is a goal that requires sufficient funding of *customers* not *providers*.”).

commitments to providing minimum data transmission speeds, such as broadband speeds of at least 1 Mbps to a majority of households within three years.<sup>43</sup>

Only by first defining what constitutes a successful program can the Commission develop policies that encourage innovation and entry by the most cost-efficient technologies and providers, and at the same time reduce overall demand on the fund. As the Mercatus Center explains, any “sound analysis of the reforms’ effect on outcomes must identify how the outcomes are to be measured and project how the reforms would cause a change in the outcomes.”<sup>44</sup> The resolution of these fundamental issues is necessary no matter what distribution model the Joint Board and the Commission ultimately employ, and should affect which model is ultimately adopted. Once the Commission has defined performance, it can allow carriers to compete to achieve these goals at the lowest cost. The benefits of this reform are likely to be enormous – as David Sappington has explained, “the competitive process, not regulatory pre-selection of a single universal service provider, is the best means to ensure the delivery of supported telecommunications services at minimum cost to consumers.”<sup>45</sup>

In sum, no reform will be “fundamental,” “comprehensive,” or “long-term” until the Commission adopts basic criteria for evaluating outputs and satisfying the objectives

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<sup>43</sup> GCI Long Term Reform Ex Parte at 8-9.

<sup>44</sup> Mercatus Center Comments at 15.

<sup>45</sup> *Federal-State Joint Board on Universal Service*, GCI Ex Parte Letters, attachment, David E.M. Sappington, *Harnessing Competitive Forces To Foster Economical Universal Service*, CC Docket No. 96-45 at 1 (filed Dec. 19, 2003) (“Sappington”) (“Among the many benefits of competition is its ability to constantly motivate industry suppliers to reduce their operating costs over time, and thereby limit the total support required to ensure the delivery of high quality services at affordable rates.”).

of high cost universal service – including defining what it means for rates to be affordable and reasonably comparable and for support to be sufficient.

**B. Limiting Support to a Single ETC Unlawfully and Irrationally Ignores the Benefits to Universal Service Provided Through Competition.**

The Joint Board’s proposal “that the POLR Fund provide support for only one carrier in any geographic area” would create a de facto ILEC-only POLR Fund, which is not only unlawful, but also bad policy.<sup>46</sup> The Commission’s proposal to limit support to a single auction winner suffers similar flaws.<sup>47</sup> Neither the Joint Board nor the Commission performs any analysis to support the notion that USF should be limited to one ETC per “geographic area,” however that may be defined. To the extent the Joint Board is proposing to support one wired (through the POLR Fund) and one wireless ETC (through the Mobility Fund) per service area, it fails even to acknowledge that the Commission previously rejected that proposal.<sup>48</sup>

There is no basis for a categorical conclusion that only a single ETC should receive support. Artificially limiting competition in this manner would not only violate the Act, but also harm rural America.

**1. Limiting Support to a Single ETC is Unlawful.**

Congress clearly contemplated that competition, not a monopoly, would best provide universal communications service. As the Senate Commerce Committee

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<sup>46</sup> *Recommended Decision*, 22 FCC Rcd at 20487 ¶ 43.

<sup>47</sup> *Reverse Auction NPRM*, 23 FCC Rcd 1495 at 1510-11 ¶ 14.

<sup>48</sup> *See Federal-State Joint Board on Universal Service*, Report and Order, 22 FCC Rcd 6371, 6396 (¶ 57) (2005) (“[W]e also decline to adopt a proposal that would allow only one wireline ETC and one wireless ETC in each service area.”).

explained more than a dozen years ago, competition is critical to achieving successful, sustainable universal service at the lowest overall cost to society:

Competition and new technologies will greatly reduce the actual cost of providing universal service over time, thus reducing or eliminating the need for universal service support mechanisms as actual costs drop to a level that is at or below the affordable rate for such service in an area.<sup>49</sup>

Since then, the courts have similarly explained that in the wake of the 1996 Act, “[t]he FCC must see to it that both universal service *and local competition* are realized; one cannot be sacrificed in favor of the other.”<sup>50</sup>

Section 214(e) of the Act expressly authorizes multiple ETC designations in a single service area and, in fact, mandates that state commissions (or the Commission where carriers are not subject to state jurisdiction) designate more than one ETC in any “non-rural” area and expressly permits states to do so in any “rural” area.<sup>51</sup> Section 214(e) does not authorize the Commission to prevent states from designating multiple ETCs or to cut-off universal service support to newly designated ETCs. Congress clearly did not view rural universal service support as a “sole source” arrangement, but, consistent with its “pro-competitive, deregulatory national policy framework,” expressly contemplated that consumers would benefit from competition in rural as well as urban areas.

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<sup>49</sup> S. Rep. No. 104-23, at 26 (1995).

<sup>50</sup> *Alenco*, 201 F.3d at 615.

<sup>51</sup> *See* 47 U.S.C. § 214 (e)(2); *see also* 47 U.S.C. § 214 (e)(1)(A) (stating that ETCs can offer services using “a combination of its own facilities and resale of another carrier’s services (including the services offered by *another* eligible telecommunications carrier)”) (emphasis added).

Yet, the Joint Board proposes to create a POLR Fund specifically to “support wireline carriers who provide this [provider of last resort] function,”<sup>52</sup> and expressly recognizes “that this single carrier recommendation eventually would *exclude* existing CETCs, some of whom are wireline CETCs.”<sup>53</sup> This directly contradicts the Commission’s previous conclusions that limiting universal service support to “only to those carriers that assume the responsibilities of ILECs” would “chill competitive entry into high cost areas” and “violate the principle of competitive neutrality.”<sup>54</sup> The Joint Board fails to present a rationale for departing from this conclusion or otherwise discuss how limiting universal support to POLRs could be competitively neutral. To the extent this is merely just a blunt cost-cutting tool, there are more defensible, equitable approaches that do not put consumers at risk.

Finally, the Joint Board POLR Fund proposal usurps the power of states that have explicitly refused to limit ETC designation to COLRs,<sup>55</sup> and ignores and discourages

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<sup>52</sup> *Recommended Decision*, 22 FCC Rcd at 20481 ¶ 11.

<sup>53</sup> *Id.* at 20487 ¶ 43 (emphasis added).

<sup>54</sup> *Federal-State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, 8857-58 (¶ 144) (1997) (“*First USF Order*”) (citation omitted); *see also id.*, 12 FCC Rcd at 8855-56 ¶ 142 (rejecting proposals to include COLR obligations on ETCs, in part, because “section 214(e) does not grant the Commission authority to impose additional eligibility criteria”); *see also Federal-State Joint Board on Universal Service*, Recommended Decision, 12 FCC Rcd 87, 170 (1996).

<sup>55</sup> Jim Chen, *Subsidized Rural telephony and the Public Interest: A Case Study in Cooperative Federalism and its Pitfalls*, 2 J. Telecomm. & High Tech. L. 307, 327 n.130 (2003) (citing Application of Smith Bagley, Inc., Docket No. T-02556A-99-0207, Decision No. 63269, Order (Ariz. Corp. Comm’n, Dec. 15, 2000); Smith Bagley, Inc., Util. Case No. 3026 (N.M. Pub. Reg. Comm’n, Aug. 14, 2001); Petition of RCC Minn., Inc. for Designation as an ETC, Docket No. UT-023033 (Wash. Util. & Transp. Comm’n, Aug. 14, 2002)). *See also* 2001 S.C. PUC LEXIS 10 (S.C. PUC 2001) (“Carrier(s) of Last Resort are ‘eligible telecommunications carriers’ as defined in Section 214(e) of the federal Telecommunications Act of 1996, but not all eligible telecommunications carriers are carriers of last resort.”).

states from finding innovative ways to share POLR responsibilities among multiple carriers, as Alaska and other states have done.<sup>56</sup> In Alaska, for example, the RCA has adopted regulations that enable it to allocate POLR obligations among multiple facilities-based local exchange carriers.<sup>57</sup>

## **2. Restricting Support to a Single Entity, whether ILEC, POLR, or Auction Winner, is Bad Policy.**

Designing a universal service support system that limits the number of ETCs in any given high-cost area is not only unlawful, but also fails to serve the public interest. Multiple ETCs should be allowed to compete to provide the lowest cost, most efficient service. Indeed, harnessing competitive markets will most effectively ensure sufficient, but not excessive, support. As former FCC Chief Economist Dr. David Sappington has explained:

[T]he competitive approach allows the market continually to identify the most efficient suppliers of supported telecommunications services, to provide appropriate incentives to those suppliers and their competitors

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<sup>56</sup> See, e.g., Alaska Admin. Code tit. 3, 53.290; Hawaii determines the carrier of last resort via a bidding process, see Haw. Code R. § 6-81-55; Missouri designated the ILEC as the COLR, but allows other LECs to apply for COLR status as well, see Mo. Code Regs. Ann. tit. 4, § 240-31.040; see also S.C. Code Ann. § 58-9-280 (contemplating the existence of multiple COLRs). Moreover, POLR/COLR is ill-defined, which will fuel the fire among states to prioritize maximum support receipts rather than create rational telecom policy. Further, it makes no sense to employ a non-uniform, 50-state COLR patchwork to administer a federal fund. At the *very* least, the Joint Board must create a common understanding of COLR and to accept that more than one carrier can meet that need – which is what Section 214(e) already provides.

<sup>57</sup> Alaska Admin. Code tit. 3, 53.290 (“The incumbent local exchange carrier is the carrier of last resort unless the commission by order changes the carrier's responsibilities under this subsection. Upon petition or on its own motion and after an opportunity for a hearing, the commission may reassign carrier of last resort responsibilities, in whole or in part, to one or more facilities-based local exchange carriers.”).

alike, to deliver universal services at minimum cost, and to continually reduce the costs and improve the quality of telecommunications services.<sup>58</sup>

Chairman Martin has similarly expressed his belief “in leveling the regulatory playing field for the purpose of fostering a competitive marketplace,”<sup>59</sup> and just recently highlighted the ability of competition to bring about “lower prices, higher usage and adoption rates, and technological innovation.”<sup>60</sup> The Joint Board and the Commission should act on this belief and mold reforms to facilitate, not stifle, market competition, giving effect to the simple truth that “the competitive process, not regulatory pre-selection of a single universal service provider, is the best means to ensure the delivery of supported telecommunications services at minimum cost to consumers.”<sup>61</sup>

GCI’s deployment to remote villages in Alaska exemplifies how competitors – receiving no more support per customer served than the ILEC, and already limited to less support overall – can enter rural markets and establish state-of-the-art services where regulation has failed to motivate the ILEC to do so. In the absence of competitive pressure from CETCs, the ILECs in these villages simply have not delivered services comparable to those available in the relatively urban areas of Alaska. The proposed reforms will perpetuate this lack of competition, leaving these rural villages at the mercy of incumbents that have so far failed to provide reliable, upgraded services. Indeed, eliminating support to CETCs, like GCI, would all but destroy innovation, competition,

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<sup>58</sup> Sappington at 18.

<sup>59</sup> Kevin J. Martin, FCC Chairman, Remarks to the National Cable and Telecommunications Association, at 5 (May 7, 2007).

<sup>60</sup> Chairman Martin’s CTIA Remarks at 2.

<sup>61</sup> Sappington at 1 (“Among the many benefits of competition is its ability to constantly motivate industry suppliers to reduce their operating costs over time, and thereby limit the total support required to ensure the delivery of high quality services at affordable rates.”).



and, ultimately, expansion of service for the very consumers the universal service fund is supposed to support.

And GCI's experience is not unique. ComspanUSA ("Comspan"), for example, delivers broadband voice, data, and video services over its own fiber facilities to rural communities throughout Oregon.<sup>62</sup> Comspan delivers "these services to those high-cost areas of the state that have largely been ignored by the incumbent local exchange carriers ("ILECs") and the local cable companies."<sup>63</sup> In previous comments, Comspan detailed its existing networks and services in rural Oregon communities and recounted how those services have put competitive pressure on ILEC and cable companies to upgrade their networks. Comspan plans to continue its expansion as the market dictates. If the proposed "reforms" exclude CETCs from support payments, however, Comspan has explained that, like GCI's planned roll-out, its "expansion plans will be stopped in their tracks, and citizens in Oregon's underserved communities will be denied precisely those benefits and services that the Act was intended to promote."<sup>64</sup> Similarly, Mid-Rivers Telephone Cooperative, Inc. ("Mid-Rivers") has reported "additional plans to continue the expansion of its facilities," including "substantially complet[ing] [its] facility overbuild in . . . six CLEC exchanges," but notes that "[t]hese plans will have to be altered if [high-cost support] is not available."<sup>65</sup>

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<sup>62</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Comments of ComspanUSA, WC Docket No. 05-337 and CC Docket No. 96-45, at 1 (filed May 31, 2007).

<sup>63</sup> *Id.*

<sup>64</sup> *Id.* at 2.

<sup>65</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Comments of Mid-Rivers Telephone Cooperative, Inc., WC Docket No. 05-337, at 5 (filed May 30, 2007).

These are just a few concrete examples of the competition and service to previously underserved or unserved areas that are sprouting from high-cost service support. Because incumbents receiving high-cost support have not yet delivered these new and innovative services, the Joint Board and the Commission cannot afford to suppress competitive efforts and deprive rural and underserved consumers – those most in need of universal service support – of the technological advances and benefits of competition. Furthermore, it is only the continued pressure of the market that can be expected to deliver the most innovative, cost-effective advanced services to rural consumers.

Regulation is simply not as effective as competition in forcing ILECs to improve service quality. As discussed above, for example, regulation alone has not compelled ACS to provide adequate service in certain communities in southeastern Alaska. Had such problems occurred after GCI had already launched its planned rural wireless service in those communities, consumers would have had an alternative network available for their use. Preventing such competition would be a disservice to the intended beneficiaries of the high-cost fund.

Furthermore, as GCI's experience demonstrates, no market is too small to benefit from competition – and the Commission need not fear artificially creating multiple networks. If a particular market, regardless of size, will not sustain more than one network, then multiple networks will not sprout. This is especially true as CETCs receive support on a per-line (or possibly in the future on a per-account) basis, which ties CETC support, both individually and collectively, directly to success in the marketplace. As Former FCC Chief Economist Dr. David Sappington notes, “in markets where scale

economies are sufficiently pronounced, the market may result in *de facto* monopoly, *i.e.*, only one firm may ultimately serve customers. But the value of *potential* entry and competition is that it allows the market continually to test whether scale economies make entry uneconomic, or whether entry is feasible and in the best interests of consumers.”<sup>66</sup> Ultimately, “[a]n absence of entry barriers,” such as those arising from a winner-take-all auction, “will help to ensure that monopoly provision arises only when such provision is in the best interests of consumers, and that competitive provision will re-emerge if the incumbent supplier ceases to pursue the best interests of consumers.”<sup>67</sup> Equally important, a regulator-sanctioned monopoly squelches any opportunity to find out whether a lower subsidy can produce the same service or whether the same subsidy can produce an even better service.

Moreover, it is important to recognize that because CETCs receive support only on a per-line basis, certifying and distributing support to more than one CETC *does not* increase total USF support.<sup>68</sup> If four CETCs collectively serve 40 % of total USF lines in a given market, the total high-cost support distributed will be the same as if only one CETC served that same 40% of total USF lines. Distributing support to multiple CETCs does not “subsidize competition” or lead to growth in the high cost fund.

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<sup>66</sup> Sappington at 16-17 (emphasis added).

<sup>67</sup> *Id.* at 17.

<sup>68</sup> Of course, where CETC offerings – like wireless family plans – generate greater numbers of payments for more “lines” (or handsets) that would normally occur with standard competitive offerings, total USF support can increase. But even this issue can be easily resolved by limiting support on a per-account basis. And this issue is not a result of designating multiple CETCs, but stems from the fact that the CETC is offering a service (additional handsets) that supplements, rather than substitutes for, the ILEC’s service.

Providing support to ILECs alone would substantially reduce marketplace discipline on ILEC services, would provide the Commission with no competitive marketplace test that it could use to determine whether ILECs were being over-subsidized through inflated costs, and would condemn rural consumers to receiving only those services the ILEC chooses to offer. TelAlaska, for example, touts itself as a “full service telecommunications provider whose roots were established in rural Alaska . . . some 35 years ago.”<sup>69</sup> In 35 years, however, TelAlaska has yet to provide wireless phone service to the rural communities it serves, despite having collected nearly \$70 million in universal service support over the past 10 years.<sup>70</sup> As OMB has confirmed, “[t]here is *no evidence* that the high cost program explicitly encourages carriers to achieve efficiencies and cost effective delivery of telecommunications services”;<sup>71</sup> the TelAlaska example simply proves this point.

If the Commission limits support to only a single ETC (or a single awardee per POLR, mobility or broadband fund), it creates an incentive for that ETC to reduce investment (if support is not related to investment, as with reverse auctions) or to “gold-plate” investment and expenses (if support is related to investment, as with “embedded costs” support). Neither result best serves the public interest. As the OMB program assessment notes:

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<sup>69</sup> Overview of TelAlaska, <http://www.telalaska.com/about/default.html>.

<sup>70</sup> See USAC Quarterly Administrative Filings to the FCC, Appendix HC01 (and its predecessors) for 3rd Quarter 1998 through 2nd Quarter 2008, available at <http://www.usac.org/about/governance/fcc-filings/>.

<sup>71</sup> Office of Management and Budget, ExpectMore, Detailed Information on the Universal Service High Cost Assessment, § 3.4 (2008) (“OMB Program Assessment”), <http://www.whitehouse.gov/omb/expectmore/detail/10004451.2005.html>.

The High Cost program subsidies generally make rural incumbent carriers whole, regardless of their investment decisions, business model, or the presence of competition in the market by guaranteeing “reasonable” rates of return . . . [a]lthough the purpose of the program is to help promote reasonably comparable rates between urban and rural areas, the extent of rate comparability needed to promote universal service is unclear.<sup>72</sup>

There is no rational basis for instituting a high cost universal service funding mechanism that would *prevent* companies like GCI from building a replacement network to provide better universal service for the same or less support than the ILEC currently receives.

**C. The Joint Board’s Approach of Separately Defining Universal Service as POLR, Mobility and Broadband is Backward-Looking and Forces the Government, not the Market, to Select Winners and Losers.**

In proposing to create three high-cost funds – a wireline POLR fund, a mobility fund, and a broadband fund<sup>73</sup> – each with only a single awardee, the Joint Board ignores the fact that modern networks increasingly provide all three services, at ever more affordable rates. GCI’s rural network, for example, will provide fundamental connectivity to fixed sites, mobility, and broadband using a combination of satellite, wireless, and wireline technology in some areas and using wireless only in other areas. It simply makes no sense to force providers to artificially “silo” technology for regulatory or support purposes when quickly evolving technology is erasing such distinctions in practice. And, as discussed, above, the approach of selecting a single awardee in each fund in each market will stymie, not promote the adoption of new technologies and services. Fundamental reform to the high cost fund should embrace new solutions for achieving universal service rather than reinforcing reliance on old technologies.

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<sup>72</sup> *Id.* § 1.4.

<sup>73</sup> *Recommended Decision*, 20 FCC Rcd at 20480-81 ¶ 11.

The Joint Board's three-fund proposal not only hinders innovation, it sacrifices competitively neutrality, and puts the state commissions in the role of selecting the winners and losers in the marketplace through their award of universal service support. In addition to hindering technological advancement and the introduction of advanced services, as discussed above, the Joint Board provides no explanation of how a single awardee would be selected, or of how the Commission could be assured that these awards would be made according to objective criteria.

Furthermore, under this proposal, ILEC-affiliated mobile providers have a big advantage, particularly where they use fixed wireless to provide the LEC service. Note that in several instances in Alaska, ILECs operate cellular systems using cellular frequencies and technologies, but call it BETRS. In those areas, ILECs would receive support for cellular networks under the POLR fund, but a non-ILEC would receive support only under the mobility fund. Such a result again illustrates the irrationality of creating artificially distinct funds where any such distinction is disappearing in the real world.

Moreover, to the extent that the Commission decides – wrongly in GCI's view<sup>74</sup> – to calculate future high-cost support based on providers' costs, separating support into three distinct funds would prove to be an administrative nightmare (assuming, of course that CETCs could even get support under the POLR fund, which seems unlikely under the Joint Board's proposal). As discussed in more detail below, even requiring CETCs and RLECs to break out their costs specifically for supported services is overly regulatory, impractical, and would raise costs to consumers. But adding to the

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<sup>74</sup> See *infra* Part V.B, C.

complexity by forcing providers to further break out costs according to the type of service deployed and/or technology used is simply unworkable. Again, GCI is an illustrative example. Since GCI plans to provide broadband, wireless, and in certain areas POLR services over the same network, it would be almost impossible to determine which costs should be apportioned to any particular fund. The Joint Board's three-fund proposal would displace market-based and technological improvements in universal service in favor of complicated and administratively wasteful top-down regulation. This would be a step backwards for universal service and American consumers.

Finally, the Joint Board's proposal to limit mobility (and broadband) fund recipients only to capital construction costs cannot be squared with the statute's command that support be "sufficient." In some areas, the potential subscriber base even for a single provider will be too small for affordable and reasonably comparably-priced subscription revenues to cover ongoing operating, management, and maintenance costs. Limiting support only to capital costs ignores this fact, dooms the USF to supporting white elephant construction that cannot be sustainably operated, and violates Section 254(e). What this will really mean is that carriers will not invest in serving these communities at all – which is directly counter to the objectives of universal service.

#### **IV. Eliminating ICLS and LSS for CETCs Only Would Violate Competitive Neutrality, Erect Barriers to Entry in Rural Areas, and Harm Universal Service.**

In the *Equal Support NPRM*, the Commission tentatively concluded that CETCs should no longer receive ICLS, and asked whether CETCs should no longer receive Local Switching Support.<sup>75</sup> Excluding CETCs from these support mechanisms would

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<sup>75</sup> *Equal Support NPRM*, 23 FCC Rcd at 1477 ¶¶ 23-24.

violate competitive neutrality and erect barriers to entry in rural areas, which would, in turn, undermine universal service by reducing marketplace pressures for incumbents to provide high quality and innovative services comparable to those available in urban areas. These problems are particularly pronounced for carriers that provide services that substitute for the ILEC's services, and therefore compete in the same product markets.

The impact of these two proposals in Alaska would be dramatic, draconian, and irrational. ICLS constitutes 44 % of ILEC support statewide, in areas such as Anchorage constitutes 100 % of the ILEC's universal service support, and in all areas far exceeds support provided under the HCLS mechanism. Eliminating ICLS alone would mean that a CETC such as GCI would, on average, have access to only about half the universal service support that an ILEC would receive for serving the same customers, even if GCI in every case ousts the ILEC from service to that customer. In individual ILEC study areas, the difference could be even more draconian – such as in Anchorage where *all* high cost support is ICLS support. Statewide, LSS is approximately 14 % of ILEC support, on average. Eliminating support for CETCs through ICLS and LSS combined would eliminate CETC access to nearly 60 % of ILEC USF support statewide. This would bring GCI's efforts to expand its own high quality service offerings outside of urban Alaska to a screeching halt – to the great detriment of rural consumers.

**A. Providing ICLS Support to Incumbents But not CETCs Cannot be Competitively Neutral and Would Harm Universal Service.**

In the *Equal Support NPRM*, the Commission tentatively concludes that ICLS should be eliminated for CETCs because CETC rates “generally are not regulated and they are not subject to SLC caps” and thus CETCs are purportedly “able to recover their revenues from end users and have no need to recover additional interstate revenues from



access charges or from universal service.”<sup>76</sup> This “analysis” can only charitably be referred to as “Alice in Wonderland” economics, with no grounding in or citation to known principles of microeconomics. This “analysis” and related tentative conclusions should be rejected.

There can be no question that ICLS was created to remove implicit support from interstate access charge rates, and to convert that support into explicit support. Prior to the creation of ICLS, the Commission capped (as it does now) the allowable federal subscriber line charges “due to affordability concerns,” but required incumbent LECs to recover additional common line costs, if at all, through per-minute carrier common line access charges imposed on long distance traffic and customers.<sup>77</sup> In the *MAG Order*, the Commission increased the permissible level of subscriber line charges, and shifted recovery of additional common line costs from the carrier common line charge to the new ICLS universal service mechanism.<sup>78</sup> The express purpose of ICLS was “ensuring that prices remain affordable.”<sup>79</sup>

The *Equal Support NPRM* posits that although the ILEC may need ICLS to achieve full cost recovery because of the SLC cap, the CETC is unregulated and thus can

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<sup>76</sup> *Equal Support NPRM*, 23 FCC Rcd at 1477 ¶ 23.

<sup>77</sup> *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers; Federal-State Joint Board on Universal Service; Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation; Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166, 16 FCC Rcd 19613, 19626 (¶ 17) (2001) (“*MAG Order*”).

<sup>78</sup> *Id.* at 19233-34 ¶ 41.

<sup>79</sup> *Id.* at 19635-36 ¶ 45.

charge a rate above the SLC cap to recover its last-mile transmission costs. The flaws in this analysis are readily apparent if one starts by examining the case in which the CETC and the ILEC have identical cost structures (as economic theory predicts would happen in the long run in a perfectly competitive market) – for example, with interstate common line costs of \$12 per line per month. The *NPRM* suggests that the ILEC would need ICLS support because it is limited, by express FCC regulation, to charging no more than \$6.50 per month for each residential line and \$9.20 per month for each multiline business line. But the *NPRM* appears then to assert that because the CETC’s rates are unregulated, the CETC could assess the full \$12.00 per month per line charge on each of its customers. This is where the analysis runs off the rails.

In the first instance, it doesn’t take an advanced degree in economics to recognize that, if the ILEC is charging (in the case of a residential customer) \$6.50 per month, the CETC will not be able to sell the same product to the same customer for \$12.00 per month. Certainly the Commission has cited no evidence that a CETC faces inelastic firm-specific demand curves when competing with the ILEC. More realistically, the CETC will be limited to charging what the ILEC can charge – \$6.50 per month. In the case of two substitute products, the Commission’s regulatory limitation on the ILEC’s price is necessarily also going to set a ceiling on the CETC’s price. Thus, both the ILEC and the CETC are limited by FCC regulation in the end-user price that can be charged, even if the limitation on the ILEC is direct and the limitation on the CETC is an outgrowth of the price limit on the ILEC. The Commission’s assertion that, in the presence of ILEC rate regulation, CETCs “are able to recover their revenues from end

users and have no need to recover additional interstate revenues from access charges or from universal service” is thus demonstrably false.

The Commission has previously recognized that subsidies to the ILEC limit the rates that CETCs can charge, even though the CETC is not regulated, and that this effective cap on CETC rates itself creates a barrier to entry:

A new entrant faces a substantial barrier to entry if its main competitor is receiving substantial support . . . that is not available to the new entrant. A mechanism that makes only ILECs eligible for explicit support would effectively lower the price of ILEC-provided service relative to competitor-provided service by an amount equivalent to the amount of the support provided to ILECs that was not available to their competitors. Thus, non-ILECs would be left with two choices -- match the ILEC's price charged to the customer, even if it means serving the customer at a loss, or offer the service to the customer at a less attractive price based on the unsubsidized cost of providing such service. A mechanism that provides support to ILECs while denying funds to eligible prospective competitors thus may give customers a strong incentive to choose service from ILECs rather than competitors. Further, we believe that it is unreasonable to expect an unsupported carrier to enter a high-cost market and provide a service that its competitor already provides at a substantially supported price.<sup>80</sup>

Surprisingly, the *Equal Support NPRM* fails even to mention or cite to the Commission's prior analysis and discussion of this highly analogous economic situation.

GCI's situation as a wireline CETC illustrates this clearly. At present, in the Anchorage suburbs of Eagle River and Wasilla, GCI charges a basic residential rate of \$9.40, plus a \$6.50 federally tariffed SLC and an Alaska Network Access Fund (the state SLC-equivalent) of \$3.00, for a total local rate plus state and federal SLCs of \$18.90 per month. This is less than what the ILEC (Matanuska Telephone Association) charges,

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<sup>80</sup> *Western Wireless Corporation Petition for Preemption of Statutes and Rules Regarding the Kansas State Universal Service Fund Pursuant to Section 253 of the Communications Act of 1934*, Memorandum Opinion and Order, 15 FCC Rcd 16227, 16231 ¶ 8 (2000) (“*Western Wireless Order*”).

which is a combined total local rate plus state and federal SLCs of \$22.70 per month. GCI is charging what the market will bear, and raising rates would likely result in GCI customers shifting to MTA. Moreover, both GCI and MTA compete to sell consumers bundled packages of voice, Internet, and video services – for which competition is fierce.

In lowest-cost disaggregation zones in Eagle River and Wasilla, GCI receives \$14.76 and \$13.55 per month in disaggregated ICLS support for residential lines.<sup>81</sup> Because MTA’s self-designated disaggregation zones were required to be “reasonably related to the cost of providing service for each disaggregation zone within each disaggregated category of support,”<sup>82</sup> the Commission can assume that MTA receives a like amount attributable to its service within these zones. In the higher-cost zones, which in Wasilla include the majority of residences, disaggregated ICLS support per residential line is \$22.97 (Eagle River) and \$23.66 (Wasilla). Plainly, even though GCI’s end user rates are not rate regulated, because MTA would continue to receive ICLS support, there is no plausible way that GCI could raise its residential rates in Eagle River and Wasilla by even \$13.55 per month (Wasilla Zone 1), let alone by \$22.97 (Eagle River Zone 2) or \$23.66 per month (Wasilla Zone 2), in order to offset the loss of ICLS support. Were GCI foolishly to attempt to do so, it would be charging a total local rate plus SLC of \$32.45 in Wasilla Zone 1, \$33.66 in Eagle River Zone 1, \$41.87 in Eagle River Zone 2, and \$42.56 in Wasilla Zone 2, all compared to MTA’s subsidized \$22.70. There is no way that GCI could do this and retain any economically rational customer. This relieves all market pressure on the ILEC to actually price its residential SLCs below the cap of

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<sup>81</sup> GCI also receives \$15.70 and \$14.36 per month in HCLS support for these lines.

<sup>82</sup> 47 C.F.R. § 54.315 (d)(2)(ii).

\$6.50 per line per month (or to lower its state-regulated rate). Consumers lose when USF support can flow only to ILECs.

Alaska carriers have already run this market test in Anchorage, only in reverse. In November 2001, when ACS persuaded the RCA to grant it both a 25 percent retail rate increase (and a substantial UNE price increase) in Anchorage, GCI held the line on its rates and gave consumers an alternative to the incumbent's business-as-usual approach. Consumers, in turn, voted with their pocketbooks and moved to GCI; GCI now serves more than 40 percent of Anchorage residential and business customers combined.

If GCI attempted to raise its rates substantially above MTA's, customers would likewise move to the lower-priced provider. There is no reason to believe the *Equal Support NPRM's* suggestion – offered without any economic analysis or support – that CLECs are somehow immune from these basic market realities.<sup>83</sup> Notably, for a substitute service, this analysis does not vary between a wireline and a wireless service. As long as the ILEC service and the CETC's service are participants in the same product market – *i.e.*, there is a high cross-elasticity of demand between the ILEC's service and the CETC's service – FCC (and state) regulation of the ILEC's end user rates will operate effectively to cap the CETC's end user rates.

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<sup>83</sup> Adding to the irrationality of its tentative conclusion, the Commission fails at all to explain why a SLC charge by an ILEC must be limited to \$6.50 for a residential customer or \$9.20 for a multiline business customer to preserve affordability, but an equivalent charge by a CETC would be “affordable” at much higher levels. “Affordability” is necessarily a demand-side, not a supply-side concept; it relates to what a consumer can afford to pay for universal service, irrespective of the identity of the provider. There is no basis for concluding that when an ILEC and a CETC are providing substitute services, that the “affordable” rate for universal service is – or rationally and logically can be – different for the ILEC and the CETC. A rate that is unaffordable for a consumer paying the ILEC is going to be equally unaffordable when paying the CETC.

Furthermore, before the creation of ICLS and the elimination of the carrier common line charge, GCI tariffed a federal subscriber line charge (residential) of \$3.50, and an interstate carrier common line charge that mirrored the carrier common line charge charged by its incumbent LEC competitors. After the *MAG Order*, GCI increased federal subscriber line charges and eliminated its interstate carrier common line charges, just as the ILEC did. With the Commission's adoption of the *CLEC Access Charge Order*, GCI cannot now go back and reinstitute an interstate carrier common line charge, as its tariffed rates are capped by ILEC rates.<sup>84</sup> GCI thus charged higher access rates before the *MAG Order* than it does today, and reduced access charges as the *MAG Order* intended and as the *CLEC Access Charge Order* later required, which was offset by ICLS support that was available to GCI. Yet the Commission is now tentatively concluding that GCI should lose this universal service support even though it cannot – by yet another FCC rule – increase its interstate access charges.

In arguing to eliminate ICLS for CETCs, some parties frequently claim that ICLS (and IAS) was support for “access” costs, and inasmuch as CMRS carriers generally do not charge access charges (because they cannot tariff interstate access charges), CMRS providers should not receive “access” support. This argument fails on several levels. First, CMRS carriers are not the only CETCs, and, as discussed above, some CETCs did and do tariff interstate access charges. But even more significantly, ICLS was adopted to shift what the Commission recognized had been an implicit universal service subsidy

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<sup>84</sup> See 47 C.F.R. § 61.26. See also *Access Charge Reform; Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, Seventh Report and Order, 16 FCC Rcd 9923 (2001) (“*CLEC Access Charge Order*”).

through interstate access charges to an explicit universal service support mechanism.<sup>85</sup> Instead of supporting interstate loop costs that could not be recovered through SLCs by assessing a carrier common in charge, the Commission collected and distributed that support through Section 254's universal service mechanisms. The Commission was required to take this action: as the United States Court of Appeals for the Fifth Circuit held in *Comsat v. FCC*, "the 'FCC cannot maintain any implicit subsidies' whether on a permissive or mandatory basis."<sup>86</sup> Once this decision was made, it is no longer possible to accurately describe this support as "access."

What ICLS clearly does is support the costs of "last-mile" transmission – the function of the ILEC loop – reducing the amount that the carrier needs to charge its end user to recover its costs. All ETCs, whether wireless or wireline, incur last-mile transmission costs. While these costs may vary between carriers, any variance should, at most, be considered in setting relative support levels; it does not provide a logical basis for categorically eliminating last-mile support for CETCs (or CMRS CETCs) altogether. Certainly, there is no relationship between whether a carrier historically charged a carrier common line charge and whether the carrier today has costs that need to be recovered from universal service support in order to preserve affordable and reasonable comparable services and rates.

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<sup>85</sup> *MAG Order*, 16 FCC Rcd at 19633 ¶ 41; *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long-Distance Users; Federal-State Joint Board On Universal Service*, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962, 12945-76 (¶ 32) (2000).

<sup>86</sup> *Comsat Corp. v. FCC*, 250 F.3d 931, 939 (5th Cir. 2001).

In adopting the universal service principle of competitive and technological neutrality, the Commission stated, “universal service support mechanisms and rules [should] neither unfairly advantage nor disadvantage one provider over another.”<sup>87</sup> Yet that is exactly what the Commission would do if it were to convert ICLS to an ILEC-only support mechanism by eliminating all support for CETCs under that mechanism.

Finally, the Commission’s tentative conclusion fails to recognize the important role that competitive neutrality in USF plays in promoting universal service overall. As discussed above, when open entry is maintained and USF is available to all ETCs, the ILECs will be under marketplace pressure to provide quality services and to continue innovating. When consumers have – or to a lesser extent at least potentially might have – a competitive alternative, the ILEC knows that if it delivers substandard service or fails to introduce new, innovative services, its competitor may well do so. By eliminating ICLS support for CETCs, the Commission would, as discussed in Section V.B., remove the competitive gas from the ILEC’s engine, reducing the ILEC’s incentive to continue to invest and to provide quality service. In that context, the regulator can only resort to command-and-control regulation to ensure that “quality services [are] available at just, reasonable and affordable rates” and that “consumers in all regions of the Nation, including . . . those in rural, insular, and high cost areas, . . . have access to telecommunications services and information services,” specifically including “advanced

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<sup>87</sup> *Federal-State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, 8801 (¶ 47) (1997) (“*First USF Order*”).



telecommunications and information services.”<sup>88</sup> Such reliance not only runs counter to the whole purpose of the 1996 Act,<sup>89</sup> but also is doomed to fail.

**B. Eliminating LSS for CETCs Would not be Competitively Neutral and Would Harm Universal Service.**

In the *Equal Support NPRM*, the Commission also asks “whether competitive ETCs should no longer receive Local Switching Support (LSS).”<sup>90</sup> While not reaching a tentative conclusion, the Commission observes, “LSS . . . includes a number of assumptions regarding switching costs, such as the economies of scope and scale, that are not likely to be accurate for competitive ETCs.”<sup>91</sup> While it is true that LSS embodies a number of assumptions about network architecture and cost structure, those can be as untrue for ILECs as for CETCs. Rather than acting in a competitively non-neutral and biased way by excluding CETCs from support, the Commission should reform LSS altogether.

LSS is a particularly arcane USF support mechanism. It is the successor to the Commission’s “Dial Equipment Minutes (DEM) weighting” mechanism in which the Commission adjusted separations factors by weighting interstate minutes of use at up to three times actual usage for the purposes of determining the separations factors applied to local switching.<sup>92</sup> The impact of both DEM weighting, and now LSS, is to provide a local telephone company an additional federal subsidy for what are presumed to be high

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<sup>88</sup> 47 U.S.C. § 254(b)(1), (3).

<sup>89</sup> S. Rep. No. 104-23, at 1 (1995).

<sup>90</sup> *Equal Support NPRM*, 23 FCC Rcd at 1477 ¶ 24.

<sup>91</sup> *Id.*

<sup>92</sup> *See First USF Order*, 12 FCC Rcd at 8892-93 ¶ 212.

switching costs per line served.<sup>93</sup> Absent local switching support, these costs would ordinarily be recovered through intrastate rates.<sup>94</sup> A CETC without access to LSS would also be at an artificial competitive disadvantage and be denied cost recovery when competing with an ILEC that receives LSS support.

Notably, unlike the HCLS mechanism, an ILEC receives LSS solely because of the size of its study area, and not as a function of the level of ILEC switching costs relative to a benchmark. All ILEC study areas below 50,000 ILEC lines can receive LSS.<sup>95</sup> This is true whether the ILEC serves that study area as part of a much larger physical network of host and remote switches, whether that study area is contiguous with other commonly-owned study areas, whether the ILEC offers other services using the same switches, and whether the ILEC's per-line costs for switching are above or below the national average. Moreover, as ILECs lose lines to competition, an ILEC can go from receiving no LSS support to receiving LSS support if it drops below 50,000 lines in a study area, again irrespective of economies of scale or scope. In short, while LSS was initially provided based on some *assumptions* about economies of scale and scope, there is no tie in the actual support mechanism between those assumptions and the receipt of LSS, whether for the ILEC or the CETC.

The Fairbanks, Alaska area provides a strong example. In the greater Fairbanks region, ACS serves the market through three different ILEC subsidiaries operating in

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<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> *See* 47 C.F.R. § 54.301 (a).

three different study areas.<sup>96</sup> Downtown Fairbanks is in one study area. Two neighboring areas, Fort Wainwright and Eielson Air Force Base, are part of another study area (ACS of Alaska - Greatland). Another part of the greater Fairbanks region, the North Pole area, is in a third study area (ACS of the Northland), which also encompasses more remote, non-contiguous Alaska villages. Despite these various regulatory groupings, however, ACS serves Fairbanks, Fort Wainwright, and North Pole through a common host/remote network, while Eielson Air Force Base has a standalone switch. The regulatory study area boundaries have nothing to do with the actual physical network architecture, or ACS's ability to aggregate nearby areas in order to capture economies of scale and scope in its Fairbanks area operations. Furthermore, if all of these neighboring areas were aggregated into a single study area and served from a single switch – as GCI does – it is not clear that any of these areas would be eligible to receive LSS support. In the past, ACS's lines in these areas taken together exceeded 50,000, and thus taken together, ACS's Fairbanks area operations would not have qualified for LSS support. Now, with ACS's line losses to GCI (and to a lesser extent to "cut-the-cord" wireless, including ACS's own wireless service) these Fairbanks areas collectively may be approaching the 50,000 line LSS threshold and may begin to qualify. But this does not reflect diseconomies of scale – just competitive failure. Indeed, it is difficult to see any rational policy reason why ILECs should qualify for USF support that they wouldn't otherwise have received simply because they have lost lines to competition. Doing so

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<sup>96</sup> ACS acquired Anchorage Telephone Utility, the non-rural municipally-owned ILEC serving the Anchorage market (now ACS of Anchorage, Inc.); Telephone Utilities of Alaska, Inc., the ILEC in Juneau (now ACS of Alaska, Inc.); PTI Communications, Inc., the ILEC in downtown Fairbanks (now ACS of Fairbanks, Inc.); and Telephone Utilities of the Northland, Inc., the ILEC serving the suburbs of Fairbanks and other, smaller areas of the state (now ACS of the Northland, Inc.).

subsidizes providers, rather than consumers, and is in direct contravention of the Fifth Circuit’s decision in *Alenco*.<sup>97</sup>

It would be highly irrational and discriminatory for ACS to receive LSS for its Fairbanks regional operations, which, except for Eielson (which has only 1600 lines), are served from a single host in Fairbanks, but for GCI – solely because it is a CETC instead of an ILEC – to receive no support for its Fairbanks regional operations, which are similarly served by a single switch in Fairbanks. Both the ACS and the GCI operations take advantage of economies of scale and scope beyond those that may have been assumed as part of (but not structurally built into) the “DEM weighting” mechanism when it was originally created. GCI does not have greater economies of scale in serving the Fairbanks region than does ACS. Indeed, because ACS has a larger market share than GCI, it is ACS, not GCI that enjoys the greater economies of scale with respect to actual lines served.

Another example is in Juneau, Alaska’s capital. Juneau is a single study area of a little over 20,000 ILEC lines. Yet 87 % of the high cost support that ACS’s ILEC receives in Juneau is from LSS. ACS and GCI each serve Juneau from a single switch, and ACS has a larger market share than GCI. Again, it would be wholly irrational and violate competitive neutrality to continue to provide LSS support to ACS in Juneau, but to withdraw that support from GCI based on some kind of “assumption” that GCI enjoys greater economies of scale and scope in switching when serving the same community. This cannot possibly satisfy the Commission’s competitive neutrality principle that

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<sup>97</sup> See *supra* n.42.

“universal service support mechanisms and rules [should] neither unfairly advantage nor disadvantage one provider over another.”<sup>98</sup>

Moreover, it also does not make sense to provide LSS to a standalone ILEC but not to a CETC that may serve the same area either on a standalone basis or as part of a larger physical network. In the first instance, because LSS is not tied to any type of cost benchmark, there is no factual basis for asserting that the ILEC’s costs per line served are actually above the CETC’s. But even more to the point, it is irrational to *discourage* carriers from achieving economies of scale and scope by using subsidies to create barriers to entry to prevent carriers from doing so. As discussed above, the Commission has previously recognized that providing an ILEC with a subsidy that is not available to the CETC creates a barrier to entry because to enter successfully, the CETC must be more efficient than the ILEC by the amount of the subsidy.<sup>99</sup> Denying CETCs access to LSS – which provides support meant to lower local service rates by subsidizing switching costs – simply discourages more efficient entry that could ultimately ensure that universal service can be provided at a lower level of subsidy for *all* ETCs, whether ILEC or CETC.

This would definitely be the case in the Alaska bush. Monthly LSS support in the Alaska bush ranges from a low of approximately \$7.50 per line per month up to over \$130 per line per month.<sup>100</sup> These amounts are significant. Eliminating LSS support for CETCs could limit the extent to which GCI could bring innovative new wireless services to bush communities, especially if the Commission were to eliminate LSS only for CETCs such as GCI and not for the ILECs competing in the same area.

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<sup>98</sup> See *supra* n.87.

<sup>99</sup> See *supra* text n.80. See also Sappington at 29.

<sup>100</sup> See USAC 2Q 2008 Appendix HC-08.

Once again, stymieing competitive entry cannot help preserve and enhance universal service. CETCs both bring new innovative services to rural and high cost areas and push ILECs to continue to improve and innovate. This dynamic benefit cannot be replicated through command-and-control regulation.

## **PART B – COMMENTS FOCUSED ON THE *EQUAL SUPPORT NPRM***

- V. Any Changes to the Equal Support Rule Should be Limited to CETCs that Predominantly do not Provide Substitutes for ILEC Services, and Should Preserve Efficiency Incentives.**
- A. Asserted Problems with the Equal Support Rule Can Be Addressed by Limiting its Application to Predominantly Substitute Services or to One Support Per Residential/Single-line business Account, and through Disaggregation.**

In the NPRM, the Commission contends that the key problem with the equal support rule is that competitive ETCs offer supported services “that were not viewed by consumers as substitutes for the incumbent LEC’s supported service.”<sup>101</sup> The FCC further explains, “[t]hese wireless competitive ETCs do not capture lines from the incumbent LEC to become a customer’s sole service provider, except in a small portion of households. Thus, rather than providing a complete substitute for traditional wireline service, these wireless competitive ETCs largely provide mobile wireless telephony service in addition to a customer’s existing wireline service.”<sup>102</sup> This caused the number of supported lines to increase significantly.<sup>103</sup> In addition, the Commission asserts that equal support “fails to create efficient investment incentives for competitive ETCs,” because the “competitive ETC has little incentive to invest in, or expand, its own

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<sup>101</sup> *Equal Support NPRM*, 23 FCC Rcd at 1471 ¶ 9.

<sup>102</sup> *Id.*

<sup>103</sup> *Id.* at 1471-72 ¶ 10.

facilities in areas with low population densities.”<sup>104</sup> Addressing these twin identified concerns, however, does not require altering equal support for ETCs that provide predominantly substitute supported services.

**1. The Commission Must Recognize the Difference Between Carriers Providing Predominantly Substitute Services, and Those Providing Predominantly Complementary Services.**

Nowhere in the NPRM does the Commission discuss the possibility that there are ETCs – like GCI – that receive support for service that essentially substitutes for traditional wireline service. There no evidence that such CETCs have contributed significantly to the growth of the High Cost Fund. If one views “wireline CETCs” as a proxy for CETCs providing predominantly substitute supported services,<sup>105</sup> total High Cost support to substitute carriers was less than \$20 million in 2007.<sup>106</sup> Indeed, there is no evidence that these CETCs are adding measurably to the total number of supported lines because when the CETC gains a line, the ILEC loses a line, and vice versa. For wireline CETCs, the total number of supported lines actually dropped by approximately

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<sup>104</sup> *Id.*

<sup>105</sup> While it is certainly possible that some wireless CETCs may be providing predominantly substitute supported services, it is unlikely that there are many such CETCs or that they would account for a significant amount of additional High Cost Support. In the most recent CMRS Competition Report, the Commission found that only approximately 11-12 % of wireless consumers nationally had “cut the cord.” *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; Annual Report and Analysis of Competitive Market Conditions with respect to Commercial Mobile Services*, 23 FCC Rcd 2241, 2340-41 (¶¶ 245-247) (2008) (“*CMRS Competition Report*”).

<sup>106</sup> Universal Service Administrative Company, High Cost Program Support Distribution by Wireline and Wireless ETCs 1999 through 4Q2007 (Jan. 23, 2008), [http://www.usac.org/\\_res/documents/about/pdf/fund-facts/HC%20Wireline-Wireless%20Distribution.pdf](http://www.usac.org/_res/documents/about/pdf/fund-facts/HC%20Wireline-Wireless%20Distribution.pdf).

25% between the first quarter of 2006 and the first quarter 2008.<sup>107</sup> In any event, in the case of substitute services, the real cause of increase in the High Cost Fund is not the entry of CETCs with support paid on a per line basis, but the Commission's own failure to implement – and ultimately its unlawful editorial deletion of – rules that required the ILEC to lose support when a line was captured by a competitor.<sup>108</sup> For this reason as well, failure to distinguish between CETCs that predominantly provide substitute supported services, and those that do not, would ignore “an important aspect of the problem” before the Commission, an outcome that would be reversible as arbitrary and capricious.<sup>109</sup>

To the extent that the Commission might remain concerned that total high cost support still increases even when a CETC provides supported services predominantly as a substitute for the ILEC, because the ILEC does not lose support when it loses a line and that ILEC support per line also thus increases as it loses lines, those problems could be addressed more simply. In 2000, the Rural Task Force proposed freezing per-line support for all ETCs (including the ILEC) at the time a CETC enters the market, and distributing support to the ILEC on a per line basis as well.<sup>110</sup> Now all high-cost support

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<sup>107</sup> Universal Service Administrative Company, High Cost Program Quarterly Line Count Totals by ILEC, Wireless CETC, and Wireline CETC 1Q2006 through 1Q2008 (Jan. 23, 2008), [http://www.usac.org/\\_res/documents/about/pdf/fund-facts/HC%20Quarterly%20Line%20Count%20Total.pdf](http://www.usac.org/_res/documents/about/pdf/fund-facts/HC%20Quarterly%20Line%20Count%20Total.pdf).

<sup>108</sup> *Federal-State Joint Board on Universal Service*, GCI Letter to Thomas Navin, CC Docket No. 96-45, at 2-5 (filed June 29, 2005).

<sup>109</sup> *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983); *see also SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947).

<sup>110</sup> *Federal-State Joint Board on Universal Service*, Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service, CC Docket 96-45, at 37 (rel. September 29, 2000). The Commission declined to adopt this proposal, saying that “the likelihood of [excessive growth in the universal service fund as a result of an



in Anchorage, Alaska, is distributed to both the CETCs (including the ILEC's CETC wireless affiliate) and the ILEC in this way.<sup>111</sup> But even if the Commission did not wish to go this far, it could address any concern about the upward spiral of CETC per-line support by simply paying the CETC support at the lower of the ILEC effective per-line support rate at the time the CETC entered the market or the ILEC's effective per line support rate at the time of payment.<sup>112</sup> This would fully address concerns about artificially increasing CETC support as a result of CETC entry to provide substitute services, while minimizing departures from the most competitively neutral outcome in which the same support is provided for the same line of universal service at the same location regardless of the identity of the provider.

**2. Limiting Support to a Single Payment Per Residential or Single-line business Account Would Substantially Reduce Support for Multiple Handsets in the Same Household.**

Even with respect to those CETCs that do not predominantly provide substitute services, the Joint Board does not address whether any problems with the current equal

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incumbent carrier's loss of lines to a CETC] occurring in the immediate future is speculative.” *Federal-State Joint Board on Universal Service; Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking in CC Docket No. 96-45, and Report And Order in CC Docket No. 00-256, 16 FCC Rcd. 11244, 11294 (¶ 123) (2001) (“RTF Order”).

<sup>111</sup> *Petition of ACS of Anchorage, Inc. Pursuant to Section 10 of the Communications Act of 1934, as Amended (47 U.S.C. § 160(c)), for Forbearance from Certain Dominant Carrier Regulation of Its Interstate Access Services, and for Forbearance from Title II Regulation of Its Broadband Services, in the Anchorage, Alaska, Incumbent Local Exchange Carrier Study Area*, 22 FCC Rcd 16304, 16307 (¶ 3) (2007) (“ACS Forbearance II Order”).

<sup>112</sup> If the ILEC is losing lines, ILEC per line support will tend to increase. However, other changes, such as increases in the Nationwide Average Cost per Loop, could cause total ILEC high cost support per line to decline over time.

support rule could be better addressed by limiting CETCs to a single support payment per residential or single-line business account. Qwest initially presented this proposal to the Joint Board in April 2007, and this proposal by itself would put an end to even the claim that CETC support is “identical” to ILEC support.<sup>113</sup> Qwest noted at the time that, according to AT&T, TNS data showed that “over 13% of supported wireless CETC lines are in households that have at least three such lines, and over 8% are in households with *four* such lines.”<sup>114</sup> Census data show such estimates are plausible. According to the 2006 Current Population Survey, the average family household had more than three members,<sup>115</sup> and the FCC in its most recent CMRS Competition Report observed, “[t]he overall wireless penetration rate in the United States is now at 80 percent, and virtually everyone in the United States between the ages of 15 and 69 has a wireless phone.”<sup>116</sup> This is also consistent with wireless marketing behavior in Alaska, where ACS Wireless

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<sup>113</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Qwest Ex Parte, attachment, Letter to Commissioners Tate and Baum, WC Docket No. 05-337 and CC Docket No. 96-45, at 3 (filed Apr. 26, 2007) (“Qwest Commissioners Letter”). It should be noted that this claim itself is false, as ILECs receive lump support based on overall reported network costs, regardless of lines actually served, while CETC support is limited to customers actually served, without regard to the network behind provision of that service.

<sup>114</sup> Qwest Commissioners Letter at 3 n.5; *see also High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, AT&T Letter to Commissioners Tate and Baum, WC Docket No. 05-337 and CC Docket No. 96-45, at 2 n. 5 (filed Mar. 22, 2007) (citing TNS data).

<sup>115</sup> See Census Bureau, *America’s Families and Living Arrangements: 2006*, Table AVG1, Average Number of People per Household, by Race and Hispanic Origin, Marital Status, Age, and Education of Householder: 2006, <http://www.census.gov/population/www/socdemo/hh-fam/cps2006.html>. According to the Census Bureau, in 2006, there were 77,402,000 family households nationwide, with an average size of 3.20 persons, and 36,982,000 households of non-family members, with an average size of 1.25 persons.

<sup>116</sup> *CMRS Competition Report*, 23 FCC Rcd at 2340 ¶ 244.

has advertised \$100 per handset credits for up to 5 additional lines added to one of its wireless accounts.<sup>117</sup>

Qwest estimated that the savings from a one payment per account rule for wireless handsets would be approximately \$500 million per year.<sup>118</sup> In that case, wireless CETC payments would be cut nearly in half. Moreover, it seems unlikely that, if the FCC were to institute a single payment per residential/single-line business account restriction, consumers would respond by establishing separate accounts. Wireless carriers all allow customers to add handsets to existing family plans at a nominal charge (usually \$10-15/month), which is far below the cost of a standalone plan.<sup>119</sup>

**3. Support Disaggregation, not Changes to the Equal Support Rule, Creates the Best Incentive for Investment in High Costs Areas.**

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<sup>117</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, GCI Ex Parte response to ACS, WC Docket No. 05-337 and CC Docket No. 96-45 (filed Feb. 11, 2008).

<sup>118</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Reply Comments of Qwest Communications International Corp., WC Docket No. 05-337 and CC Docket No. 96-45, at 3 (filed July 2, 2007).

<sup>119</sup> Verizon Wireless, Nationwide Basic Family SharePlan®, (2008), <http://www.verizonwireless.com/b2c/store/controller?item=familyShare&action=viewFSPlanList&sortOption=priceSort&typeId=2&subTypeId=22&catId=323>; AT&T, FamilyTalk 700 (2008), [http://www.wireless.att.com/cell-phone-service/cell-phone-plan-details/?q\\_sku=sku1250110&q\\_planCategory=cat1370013&cnt=1](http://www.wireless.att.com/cell-phone-service/cell-phone-plan-details/?q_sku=sku1250110&q_planCategory=cat1370013&cnt=1); Sprint Nextel, Sprint Power Pack Family Plans (2008), <http://nextelonline.nextel.com/NASApp/onlinestore/en/Action/DisplayPlans>; T-Mobile, myFaves for Families 700 (2008), <http://www.t-mobile.com/shop/plans/detail.aspx?tp=tb1&id=3e939aa9-5d54-4f6b-a34b-b91adfc9ddd8>; ACS, ACS Wireless Plans, Family Plans (2008), <http://www.acsalaska.com/Cultures/en-US/Personal/Wireless/Plans+Features+and+Options.htm>; Matanuska Telephone Association, Call Alaska Plan, Call Nationwide Plan (2008), <http://www.mta-telco.com/wireless/plans.html#n>.

In addition, changing the equal support rule is not necessary to create incentives to invest in service to the high cost portions of a study area both for CETCs that predominantly substitute for ILEC supported services and for other CETCs, particularly if the Commission also limits support to one payment per residential or single-line business account. Those incentives to invest in serving high-cost portions of the study area can be and already are achieved through support disaggregation. This is particularly true when a CETC is serving the entire ILEC study area.

As adopted by the Commission in its *Rural Task Force Order*, disaggregation allows the ILEC and/or the state commission to deaverage CETC support paid per line within the ILEC study area.<sup>120</sup> Although the *RTF Order* required ILECs to make an election, that election is always subject to change by the state commission (or by the FCC for entities not subject to state commission jurisdiction).<sup>121</sup> The general principle of disaggregation is that disaggregation will reflect underlying cost variations. For the most commonly selected option, Path 3, in which an ILEC had the option to self-certify a disaggregation plan with two zones per wire center, the Commission expressly required that disaggregation reflect the underlying cost of providing service.<sup>122</sup> FCC rules also expressly allowed the ILEC to self-certify a benchmark system for support, which could

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<sup>120</sup> *RTF Order*, 16 FCC Rcd. at 11303-04 (¶¶ 149-151); 47 C.F.R. § 54.315. Because ILECs do not receive per line support for the programs subject to disaggregation (HCLS, LSS and ICLS), disaggregation only affects CETC support. See 47 C.F.R. § 54.315 (e)(7). ILECs continue to be paid based on aggregate study area costs and line counts.

<sup>121</sup> 47 C.F.R. § 315 (b)(4), (c)(5), (d)(5).

<sup>122</sup> 47 C.F.R. § 315 (d)(2) (“[T]he plan must be reasonably related to the cost of providing service for each disaggregation zone within each disaggregated category of support.”).

result in no support for some areas while focusing all support on others.<sup>123</sup> For Path 2 disaggregation, the Commission did not establish such an explicit requirement, but that was only because Path 2 disaggregation was subject to express state commission oversight and approval to ensure competitive neutrality.<sup>124</sup> Notably, under Path 2, a state commission can approve disaggregation at as granular a level as the state commission deems appropriate.

With disaggregation, a CETC that serves only the low cost parts of the study area can receive little or no support. Thus, if the ILEC or state commission establishes a disaggregation system with little or no support in the low cost core, the CETC cannot expand its USF support substantially simply by serving those areas. On the other hand, when support is substantially deaveraged and disaggregated, the CETC gains much more support if it invests to serve the disaggregation zones that receive high levels of support. In the Matanuska Valley in Alaska, for example, MTA has established disaggregation zones that range from \$0 in support per line per month in Willow Zone 1 to \$80.81 per residential/single-line business line per month in Cantwell Zone 2.<sup>125</sup> In this situation, a CETC has a substantial incentive to build-out its networks in hard-to-serve higher-cost areas, and not to concentrate its efforts in more densely populated lower-cost areas. The NPRM fails to address disaggregation when discussing CETC incentives to invest under the equal support rule. This is another important dimension of the issue that cannot be ignored, lest the Commission act arbitrarily and capriciously.<sup>126</sup>

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<sup>123</sup> See *RTF Order*, 16 FCC Rcd at 11304 ¶ 151; 47 C.F.R. § 54.315 (d)(2)(iv).

<sup>124</sup> See *id.*, 16 FCC Rcd at 11304 ¶ 150.

<sup>125</sup> Universal Service Administrative Company, Second Quarter 2008, Appendix HC-04.

<sup>126</sup> See *infra* n.149.

There are, of course, some instances where disaggregation may not work well at present. For example, if the ILEC elected Path 1 and then a CETC entered, there would be no disaggregation. The existing rules, however, allow the state commission or the FCC to address this issue by creating a disaggregation plan. Thus, any distorted investment incentives resulting from the ILEC's Path 1 election can be corrected now within the existing disaggregation framework.

As another example, an ILEC may have designed its self-certified Path 3 disaggregation plans so as to allow it to maximize the USF support received by an affiliated CETC. Again, the existing rules allow the state commission or the FCC to address this issue by modifying the disaggregation plan. In addition, to the extent that the Commission also adopted a one payment per residential and single-line business account rule, the opportunity for the affiliated CETC to derive substantial revenue through a distorted disaggregation plan would be substantially lessened.

It is important for the Commission to recognize that there are better ways to address its concerns with the equal support rule, and that it need not shift to an "own costs" support mechanism. As discussed further below, "own costs" support has significant costs of its own. Most significantly, "own costs" will substantially blunt marketplace forces in promoting the delivery of cost-effective and efficient universal service, predictably leading to excessive, not sufficient, universal service support. When all ETCs, including both the ILEC and the CETC, are paid on the basis of "own costs" up to a ceiling of the ILEC's support, as the NPRM proposes, neither the ILEC nor the CETC has an incentive to become more efficient and to pass those savings on to either consumers or the USF. In addition, an "own costs" mechanism will entail the creation

and enforcement of substantial bureaucracy that is unnecessary when ETCs are competing to provide substitute services, and will create enormous and unnecessary paperwork burdens, violating both the Regulatory Flexibility and Paperwork Reduction Acts.

**B. The Commission Must Recognize that Replacing the Equal Support Rule with an “Own Costs” Mechanism Will not only Violate Competitive Neutrality, But also Lead to Excessive and Inefficient Support.**

While the Commission could make some changes to the equal support rule – such as limiting CETC’s but not ILECs to a single support payment per residential or single-line business account – that would only modestly infringe upon competitive neutrality while addressing the Commission’s policy concerns identified in the *Equal Support NPRM*, moving to an “own costs” mechanism would obliterate competitive neutrality as an objective of universal service policy and would significantly blunt the ability of the market to drive the cost-effective delivery of universal service. Neither of those results is in the public interest.

The costs of the “own costs” approach are three-fold:

- Instituting “own costs” regulation for CETC in essence puts all universal service providers on rate-of-return regulation, which the Commission has long recognized leads to inefficient operations – and therefore excessive, not merely sufficient, universal service support.
- Instituting “own costs” support for CETCs protects the ILECs against any marketplace consequences of inefficiency. The “own costs” support mechanism will prevent the market from revealing the extent of ILEC inefficiency and over-subsidization, except in a very extreme case.
- “Own costs” will require the creation of complex cost allocation rules that are difficult to implement, administer and enforce, and that are wholly unnecessary for any other regulatory purpose (unlike ILEC cost accounting, which is necessary for both price regulation and to prevent anticompetitive cross-subsidization and cost misallocation).

It should be beyond cavil that “own costs” USF amounts to little more than rate-of-return regulation applied to CETCs. The Commission clearly contemplates that CETCs would report their costs according to some kind of accounting regime, and that the amount of CETC support would be determined according to the same algorithms as the ILEC. As the NPRM also recognizes, this requires prescribing a rate of return for CETCs – which the Commission proposes to set at 11.25%.<sup>127</sup> As a form of rate-of-return regulation, “own costs” suffers the same flaws as ILEC rate-of-return regulation: “rather than encourage socially beneficial behavior by the regulated firm, rate of return [regulation] actually discourages it.”<sup>128</sup> As the Commission has explained:

The distorted incentives created by rate of return regulation are easily illustrated. In a competitive environment, where prices are dictated by the market, a company’s unit costs and profits generally are related inversely. If one goes up, the other goes down. Rate of return regulation stands this relationship on its head. Although carriers subject to such regulation are limited to earning a particular *percentage* return on investment during a fixed period, a carrier seeking to increase its dollar earnings often can do so merely by increasing its *aggregate* investment. In other words, under a rate of return regime, profits (i.e., dollar earnings) can go up when investment goes up. This creates a powerful incentive for carriers to ‘pad’ their costs, regardless of whether additional investment is necessary or efficient. And, because a carrier’s operating expenses generally are recovered from ratepayers on a dollar-for-dollar basis, and do not affect shareholder profits, management has little incentive to conserve on such expenses.<sup>129</sup>

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<sup>127</sup> *Equal Support NPRM*, 23 FCC Rcd at 1475-76 ¶ 18.

<sup>128</sup> *Policy and Rules Concerning Rates for Dominant Carriers*, Report and Order and Second Further Notice of Proposed Rulemaking, 4 FCC Rcd 2873, 2889 (¶ 29) (1989) (“*AT&T Price Cap Order*”).

<sup>129</sup> *Id.*, 4 FCC Rcd at 2889 ¶ 30 (emphasis added); see also *Policy and Rules Concerning Rates for Dominant Carriers*, Second Report and Order, 5 FCC Rcd 6786, 6790 (¶ 30) (1990) (“*LEC Price Cap Order*”) (“Unfortunately, a regulatory system that simply corrects for a tendency to pad investments or expenses is not a system that can also drive LECs to become more efficient and productive. But incentive regulation, by limiting the amount carriers can charge for their services and continually exerting downward pressure on those price ceilings, can.”).



To be sure, the Commission asks whether it should create a ceiling on CETC per-line support.<sup>130</sup> The Commission in fact acknowledges that, under an “own costs” mechanism, CETC’s (like rate-of-return regulated ILECs) would have an incentive “to inflate their costs.”<sup>131</sup> But that incentive is there even if the Commission were to cap CETC support at the ILEC’s effective per line support level. At all levels below the ILEC’s effective cost per line, CETCs would have the incentive to inflate costs and to become more *inefficient* in order to maximize the amount of universal service support received.

These incentives are easily illustrated. Suppose that a rate-of-return ILEC had reported loop costs of \$40 per line per month (at an 11.25% rate of return), and on that basis received \$20 per line per month in USF support in order to permit the ILEC to charge a \$20 retail rate. Further suppose that a CETC could provide the same universal service for \$30 per month, but because it receives support based on its own costs, receives only \$10 per line in USF support, in order to reach a \$20 retail rate (\$30 in costs - \$20 in retail rate = \$10 in USF support). In this situation, there is absolutely no incentive for the CETC to become more efficient. If the CETC becomes more efficient, it loses support. Indeed, the CETC will increase its universal service support if it increases its costs. So if the CETC’s costs rise from \$10 to \$15, the only effect in the market is that the CETC’s universal service support will increase by \$5 per line per month.

This example illustrates the second problem with distributing support to CETCs based on their “own costs” – the lack of any marketplace mechanism to force the ILEC to

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<sup>130</sup> *Equal Support NPRM*, 23 FCC Rcd at 1478 ¶ 25.

<sup>131</sup> *Id.*

become more efficient. In this same example, the USF fully insulates the ILEC against any adverse marketplace consequences of inefficiency. Although the CETC is \$10 per line more efficient than the ILEC, the CETC cannot exploit that advantage because its efficiency advantage is wholly offset by the increased universal service support the ILEC receives. If the CETC had received the same amount of support as the ILEC (\$20 per line per month), the CETC might be able to price its service closer to \$10 per line per month, which would put pressure on the ILEC to lower its own end user rates.

Regulators could then observe the trend of those rates, and use that information to adjust the amounts of universal service support. Under “own costs,” however, regulators and the market are denied this type of marketplace feedback. Instead, the USF ratepayers nationwide simply pick up the tab for the ILEC’s inefficiency. In this manner, basing CETC support on the CETC’s own costs will predictably lead to excessive, rather than merely sufficient, USF support, which would itself violate the Act.<sup>132</sup>

Economists have long recognized the extent to which regulation — especially rate-of-return regulation — is unlikely to be ideal, and the degree to which competition is superior as an alternative to regulation. As Alfred Kahn noted more than thirty years ago:

Regulated monopoly is a very imperfect instrument for doing the world’s work. It suffers from the evils of monopoly itself – the danger of exploitation, aggressively or by inertia, the absence of pervasive external restraints and stimuli to aggressive, efficient and innovative performance. Regulation tends inherently to be protective of monopoly, passive, negative, and unimaginative. . . . Regulation is ill-equipped to treat the more important aspects of performance – efficiency, service innovation, risk taking, and probing the elasticity of demand. Herein lies the great

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<sup>132</sup> See *infra* n.44.

attraction of competition: it supplies the direct spur and the market test of performance.<sup>133</sup>

Furthermore, as Clair Wilcox wrote, “[r]egulation, at best, is a pallid substitute for competition. It cannot prescribe quality, force efficiency, or require innovation, because such action would invade the sphere of management. But when it leaves these matters to the discretion of industry, it denies consumers the protection that competition would afford.”<sup>134</sup> By blunting the operation of a competitive market, distributing universal service based on each carrier’s costs marches backward into command-and-control regulation, and dulls the efficiency, service innovation and risk taking that would otherwise benefit America’s rural consumers. This alone would condemn rural America to a second-class communications infrastructure.

### **C. “Own Costs” Support is Unnecessarily Burdensome.**

In addition to creating incentives for inefficiency (and thus making it unlikely that the rate-of-return ILEC will operate efficiently), “own costs” support for CETCs imports into the USF system the same administrative cost and enforcement difficulties that led the FCC to move away from rate-of-return regulation for ILECs. As the Commission concluded in its first price cap order:

[A]dministering rate of return regulation in order to counteract these incentives [to ‘pad’ costs, including operating expenses] is a difficult and complex process, even when done correctly and well. This is so primarily for two reasons. First, such regulation is built on the premise that a regulator can determine accurately what costs are necessary to deliver service. In practice, however, a regulator may have difficulty obtaining accurate cost information as the carrier itself is the source of nearly all information about its costs. Furthermore, no regulator has the resources to

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<sup>133</sup> Alfred E. Kahn, *The Economics of Regulation: Principles and Institutions. Volume I*. New York: John Wiley & Sons (1970) at 325-326.

<sup>134</sup> Clair Wilcox, *Public Policies Toward Business, Third Edition*, 476-477 (1966).

review in detail the thousands of individual business judgments a carrier makes before it decides, for example, to install a new switching system.

The second inherent difficulty associated with administering rate of return regulation relates to its requirement that determinations be made about how to allocate a carrier's costs among service that often are provided jointly or in common. Such determinations tend to become more economically problematic as they become more detailed. The history of this Commission's experience in this area over the past several decades reflects the difficulty of implementing cost allocation systems.<sup>135</sup>

There is nothing about "own costs" USF support that makes the Commission's earlier observations any less true today.<sup>136</sup>

There can be no mistaking the overwhelming regulatory paperwork burden that the Commission would create by implementing an "own costs" mechanism. This is not just a matter of taking numbers from a CETC's existing income statements and balance sheets, but would require a whole new set of rules governing accounting, cost allocation and even documentation. Although the authors of the WiCAC proposal<sup>137</sup> pretend that it would be a simple thing to map a CETC's costs into 23 Part 32 accounts, the Commission's own questions reveal the many hidden complexities.

For example, the Commission asks whether, "because competitive ETCs will, in general, operate in multiple study areas of incumbent carriers, it will be necessary to disaggregate each competitive ETC's cost by relevant competitive ETC service area, and

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<sup>135</sup> *AT&T Price Cap Order*, 4 FCC Rcd at 2889-90 ¶¶ 31-32.

<sup>136</sup> Recent evidence also suggests that incentive regulation, without competition, is not sufficient to foster substantial cost reductions in the U.S. telecommunications industry. However, cost reductions do occur, when incentive regulation is combined with competition. Chunrong Ai and David E. M. Sappington, *The Impact of State Incentive Regulation on the U.S. Telecommunications Industry*, *Journal of Regulatory Economics*, 22(2), 133-159 (Sept. 2002).

<sup>137</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, GVNW Ex Parte and attached WiCAC proposal, WC Docket No. 05-337 and CC Docket No. 96-45 (filed Sept. 19, 2007) ("WiCAC proposal").

by the relevant incumbent LEC study area, wire center, or disaggregation zone.”<sup>138</sup>

Setting aside the issue of whether it is necessary to track costs below the level of the ILEC study area (it is not, as discussed further below), as the Commission recognizes, this requires cost allocation rules, particularly for costs that cannot be directly assigned to service in a particular area. The Commission proposes one possible rule – to allocate all costs not maintained in separate books of account on the basis of active telephone numbers or customers.

This rule would itself be irrational – and inexplicably varies from the rules applicable to the ILECs. To use GCI as an example, when GCI finishes its rural wireless deployment, it will operate in 27 ILEC study areas, the largest of which – and the area with the greatest teledensity – is Anchorage, which has nearly 40 percent of the state’s wireline telephone lines. In the absence of separate books of account, the NPRM apparently proposes that all of GCI’s statewide costs wherever incurred would be allocated disproportionately to Anchorage – even though it is a lower cost area. This would produce a cost allocation that has nothing to do with cost causation: higher costs of loops in the Alaska bush or even Alaska’s other communities, or the costs of flying in repair and maintenance crews to bush communities, do not increase the costs of serving Anchorage.

The impact of this cost allocation formula is particularly perverse, and undermines the Commission’s stated investment concerns for pursuing “own costs” support in the first place. Allocating GCI’s statewide costs by lines would overallocate costs to the Anchorage study area, increasing the amount of universal service support that

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<sup>138</sup> *Equal Support NPRM*, 23 FCC Rcd at 1474-75 ¶ 16.

GCI would receive for serving Anchorage – further increasing the incentive to invest and focus marketing resources in Anchorage. On the other hand, the formula would underallocate costs to higher cost areas, reducing the amount of support for serving the truly high cost areas. This *reduces* rather than *increases* the incentive to invest and market in high cost areas. This type of cost allocation and skewed universal service support mechanism would only make sense in Wonderland.

Moreover, contrary to the NPRM’s assumption, separate books of account (and separate affiliates) do not make the cost allocation issues disappear. To the contrary, cost allocation rules remain necessary to allocate investment. Some investment, such as wire loops, may be easily allocable directly to service in a particular geography. Cell towers, on the other hand, could in some instances be split between areas. Switches may serve a single ILEC study area, or may serve multiple ILEC study areas. Customer service, repair and maintenance facilities and assets all will need to be allocated and assigned to different areas. ILECs prepare cost allocation manuals to document these allocations. In an “own costs” world, just to be able to defend themselves in an audit, CETCs would have to compile something similar.

Furthermore, as the NPRM also recognizes, a CETC’s network will not necessarily duplicate the ILEC’s network topology. Thus, the Commission will be faced with answering questions about how to classify investments in the CETC’s network that may be analogous to more than one ILEC investment category. This could require another set of rules, unless the Commission simply accepts the CETC networks as it finds them, and doesn’t try to “force fit” CETC networks into ILEC cost accounting categories

such as “loop”, “switch” and “transport.”<sup>139</sup> Notably, the WiCAC proposal only purports to address a portion of this problem. While WiCAC proposes a part of a wireless support calculation mechanism (entirely ignoring underlying cost allocation issues), WiCAC does not begin to address other network topologies, such as cable or other CLEC networks, other than to say that these networks should comply with the existing ILEC Parts 32, 64 and 36 regulations.<sup>140</sup> In addition to being wildly over-regulatory and ignoring the differences among existing networks also pose, WiCAC ignores evolving networks, like GCI’s, that may use wireless, cable or a combination of both to serve a particular ILEC study area.

The NPRM also fails to consider what documentation might be required. Would CETCs be directly or indirectly required to maintain, for example, continuing property records to document deployment of specific assets (loops, switches, trunks, towers, trucks, etc.) in specific ILEC study areas? Questions like this illustrate the vast potential for regulatory complexity arising from any “own cost” mechanism that attempts to track CETC embedded costs.

Moreover, these accounting requirements would not serve any regulatory purpose other than determining USF support. For CETCs, unlike ILECs, these accounting rules would not be used to set end user or access rates.<sup>141</sup> They are not necessary to police anti-competitive cross-subsidization. Own costs would require an extraordinarily

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<sup>139</sup> As discussed further below, this approach – to accepting CETC networks as it finds, not introducing even more rules – is the right approach for the Commission to adopt.

<sup>140</sup> See generally WiCAC Proposal, “Frequently Asked Questions” at 2.

<sup>141</sup> Even when a CETC rate is regulated, such as with CLEC access charges, the CETC is subject to a cap based upon the ILEC’s (or in some cases, NECA’s) tariffed access rate, and not on cost studies. See 47 C.F.R. § 61.26; see generally *CLEC Access Charge Order* 16 FCC Rcd at 9923.

burdensome regulatory superstructure for a single purpose, despite the availability of far less burdensome (and more effective) alternatives.

The Commission should not be deceived into believing that the necessary cost allocations can simply be derived from existing corporate books of account kept in accordance with Generally Accepted Accounting Principles – or that this process is somehow made manageable by specifying “only” 23 accounts. GCI has no “service-driven”<sup>142</sup> or any other business reason to attempt to segregate each and every investment and expense dollar to specific ILEC study areas or to the functional classifications in Part 32 or in the WiCAC proposal.<sup>143</sup> AT&T Mobility’s experience confirms these obstacles:

- “AT&T Mobility books costs based on ‘market clusters’ which can encompass multiple and/or partial states,” not by ILEC study area.
- “Financial accounting is based on business needs and development of [wireless carriers’] networks.”
- Even WiCAC’s more limited Part 32 categories still require fundamentally different accounting. “Thus, for example, instead of recording wages and salaries in the wages and salaries expense account used by AT&T Mobility, wages and salaries would have to be assigned or allocated among the different functional accounts” used in the WiCAC proposal – or in any similar Part 32-like structure.<sup>144</sup>

The Commission would be imposing nothing less than a whole new set of accounting and cost allocation requirements on carriers that have never been subject to such obligations – and for whom such obligations serve no purpose other than calculating USF support.

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<sup>142</sup> *Vonage Holdings Corporation Petition for Declaratory Ruling Concerning an Order of the Minnesota Public Utilities Commission*, Memorandum Opinion and Order, 19 FCC Rcd 22404, 22419-21 (¶ 25) (2004).

<sup>143</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, GVNW Ex Parte and attached WiCAC Proposal, WC Docket No. 05-337 and CC Docket No. 96-45 (filed Feb. 20, 2008).

<sup>144</sup> WiCAC Proposal.



ACS Wireless, in its comments to the Joint Board, underscored the difficulties in developing an “own costs” support mechanism for CETCs. As ACS noted, “Wireless carriers’ plant and operations accounts and accounting practices vary from ILECs’ significantly because wireless carriers’ operations, network designs, and revenues are different from ILECs’,” necessitating the development of a completely different accounting system for wireless carriers.<sup>145</sup> Similarly, “the FCC will have to develop parallel rules [to the Commission’s Part 64 and Part 36 rules] for wireless carriers to identify specific costs that underlie provision of basic universal services.”<sup>146</sup> ACS correctly assesses that “[r]eplicating these rules will be no simple task.”<sup>147</sup>

The NPRM, in proposing to eliminate the Equal Support Rule, fails to take any of these well known and previously well-recognized costs into account. Once again, were the Commission to ignore these costs, it would fail to address a critical aspect of the issue before it and would likewise fail to explain its abrupt deviation from the Commission’s earlier analysis of rate-of-return regulation in the Commission’s price cap orders.

**D. The Commission Should Reject Plainly Discriminatory Proposals.**

The Equal Support NPRM contains several proposals that plainly discriminate against CETCs, and should be discarded on that basis. The Commission cannot reconcile these proposals with its own principle of competitive and technological neutrality.

**1. The Commission Should Not Require Preapproval of CETC Cost Support or Suspend CETC Support Pending Completion of Cost Reviews by the FCC or the States.**

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<sup>145</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Comments of ACS Wireless, Inc., WC Docket No. 05-337 and CC Docket No. 96-45, at 6 (filed May 31, 2007).

<sup>146</sup> *Id.* at 7.

<sup>147</sup> *Id.*

The NPRM tentatively concludes that CETCs' cost studies would have to be approved by the state commission or the FCC before such information could be filed with USAC, presumably delaying the use of such cost studies until that time.<sup>148</sup> Although the Commission holds out the possibility that CETCs could update costs on a quarterly basis – as rural ILECs do – such updates also appear to require approval by the state commission or FCC.<sup>149</sup>

This tentative conclusion strikingly varies from the existing requirements for ILECs. Nothing in Part 36 or Part 54 requires FCC or state approval of ILEC cost studies before those cost studies may be submitted to NECA and/or USAC as the basis for ILEC high cost support. While there may be an assumption that these ILEC cost studies are reviewed in other contexts, that assumption is not necessarily true. Some ILECs are not regulated at all by state commissions with respect to their end user rates, and other ILECs have rates set by alternative regulation plans that do not require review of cost studies. As an example, in Alaska, in any study area that is competitive, Alaska ILECs have no regulatory limits on their rates other than the basic residential service rate – and even the cap on that rate expires in 2010.<sup>150</sup> Even when state commissions are empowered to conduct traditional cost-of-service rate cases, states do not conduct those cases every year, let alone quarterly. At the federal level, the FCC does not review individual ILEC cost studies when those ILECs are members of the NECA pool. And even for companies that are not in the NECA pool, detailed review of ILEC cost studies only occurs when

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<sup>148</sup> *Equal Support NPRM*, 23 FCC Rcd at 1473 ¶ 13.

<sup>149</sup> *Id.*

<sup>150</sup> Alaska Admin. Code tit. 3 § 53.243.

there is a full tariff investigation – which is rare. In almost all cases, ILEC federal tariffs take effect on no more than 15 days notice.<sup>151</sup> Thus, the Commission relies on ILECs to provide accurate cost studies without preapproval by any regulatory body.

The NPRM sets forth no rationale for treating CETCs more stringently than the ILECs who receive three-quarters of all high cost support. To the extent that known problems with ILEC cost studies underlie the CETC pre-approval requirement, the D.C. Circuit has rejected as arbitrary and capricious similar reasoning in an analogous case where the Commission required interconnected VoIP providers to obtain FCC pre-approval of USF traffic studies, but placed no similar requirement on CMRS carriers.<sup>152</sup> To place a cost study pre-approval requirement on CETCs but not ILECs would be equally invalid.

Furthermore, requiring CETC cost study pre-approval before such cost studies could be used as the basis for universal service support would be highly disruptive to those CETCs already serving high cost areas, and would create a substantial and unpredictable lag for CETCs that are building out. There is no good reason to interrupt the flow of universal service support payments to CETCs serving rural and high cost areas while cost studies are reviewed. As with ILECs, if the FCC doubts the validity of these studies, it can conduct audits and recover any support that was erroneously provided. Similarly, for new entrants, the Commission has already recognized that lack

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<sup>151</sup> See 47 U.S.C. § 204 (a)(3).

<sup>152</sup> *Vonage Holdings Corp. v. FCC*, 489 F.3d 1232, 1244 (D.C. Cir. 2007) ("The Commission's explanation thus gives us no confidence that it has apportioned USF obligations on 'an equitable and nondiscriminatory basis.'").

of access to high cost support creates a barrier to entry.<sup>153</sup> Failing to commence high cost support during a review and approval process of indeterminate length means that a CETC will be subject to a long delay before it knows how much universal service support it will receive if it serves a particular area. Such indeterminacy can hardly be said to constitute “specific, predictable and sufficient Federal . . . mechanisms to preserve and advance universal service.”<sup>154</sup>

**2. The Commission Should not Refuse to Permit CMRS Providers to Obtain Support for the Cost of Capital Expended for Auctioned Spectrum.**

In one of its more perplexing proposals, the NPRM suggests that CMRS providers may not be permitted to recover a return on their investments in acquiring spectrum, as if spectrum auction payments were an expense and not an investment expenditure to be included in the ratebase.<sup>155</sup> The NPRM provides no rationale for this approach, which is clearly contrary to the economics of acquiring spectrum. Buying spectrum is like buying land (Account 32.2111). Land is expressly included in Telecommunications Plant in Service (Account 32.2001), which is part of a carrier’s ratebase.<sup>156</sup> The Commission has never suggested that carriers should not be permitted a return on investment (*i.e.*, a recovery of the cost of capital) on their investments in land. Inasmuch as there appears to be no rational basis for treating spectrum differently than land, it would be arbitrary and capricious to deny CETCs a return on their spectrum investments.

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<sup>153</sup> *Federal-State Joint Board on Universal Service; Western Wireless Corporation Petition for Preemption of an Order of the South Dakota Public Utilities Commission*, Declaratory Ruling, 15 FCC Rcd 15168, 15173 (¶ 13) (2000); *see also Western Wireless Order*, 15 FCC Rcd at 16231 ¶8.

<sup>154</sup> 47 U.S.C. § 254 (b)(5), (d), (e).

<sup>155</sup> *Equal Support NPRM*, 23 FCC Rcd at 1476 ¶ 20.

<sup>156</sup> 47 C.F.R. §§ 65.800, 65.820.

### **3. The Commission Should Reject WiCAC's Proposed Algorithm for Determining Wireless CETC High Cost Support.**

In the NPRM, the Commission notes that WiCAC has proposed using 23 specific Part 32 accounts to calculate wireless competitive ETC costs.<sup>157</sup> As discussed above, implementing this proposal would require CETCs to install whole new cost accounting systems, and would impose a regulatory superstructure for the sole purpose of determining universal service support. The WiCAC proposal can hardly be said to be a “pro-competitive, deregulatory” approach, and thus is wholly out of step with the purpose and intent of the 1996 Act.

In addition, the Commission should reject WiCAC's proposed algorithm because it puts a “thumb on the scales” to deliberately bias downward CETC support calculations. WiCAC does this by including what it calls the “intraMSA” factor. This factor uses the ratio of intraMSA or, outside of MSAs, intra-study area<sup>158</sup> MOUs to total MOUs to create a factor by which to reduce the allocation of costs to “loop” facilities supported by USF, and also proposes a default value of 50%. WiCAC sponsors allege that this factor will help distinguish “loop” from “transport.”<sup>159</sup> But as AT&T has pointed out, the effect of the “intraMSA” factor is “to artificially reduce wireless carriers’ costs...in a manner more likely to exclude wireless ETCs from receiving support.”<sup>160</sup>

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<sup>157</sup> *Equal Support NPRM*, 23 FCC Rcd at 1473-4 ¶ 15.

<sup>158</sup> Presumably the WiCAC sponsors mean the ILEC study area.

<sup>159</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, GVNW Ex Parte Letter, WC Docket No. 05-337 and CC Docket No. 96-45, at 3 (filed Nov. 7, 2007).

<sup>160</sup> *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, AT&T Ex Parte, attachment, WC Docket No. 05-337 and CC Docket No. 96-45, at 4 (filed Nov. 9, 2007).

AT&T is clearly correct. In the first instance, WiCAC sponsors offer no reason why “intraMSA” or “intra-study area” endpoints are relevant to distinguish “loop” equivalent costs from “transport” equivalent costs. For the HCLS mechanism, all loop costs are included in the HCLS calculation, not just the proportion of loop costs that could be attributable, on an MOU basis, to “local” traffic. The HCLS mechanism supports *unseparated* loop costs, which means that the end points of the traffic traveling over the loop are irrelevant. Second, even if there were some rational basis for limiting support to loop costs attributed to “local” traffic on the basis of MOUs, the Commission has clearly ruled, in its reciprocal compensation rules, that for CMRS traffic all intraMTA traffic is treated as local.<sup>161</sup>

The arbitrariness and result-oriented nature of WiCAC’s proposed intraMSA factor shows up throughout its proposed USF support algorithm. WiCAC proposes, for example to apply the intraMSA factor to spectrum costs (*i.e.*, the costs of purchasing auctioned spectrum). But that spectrum is purchased for the specific purpose of providing last mile transmission from the cell tower to the subscriber’s location. This is directly analogous to the ILEC’s copper loop plant and associated rights of way. The same is true for the towers themselves, which WiCAC proposes to include in an account entitled “Wireless Transmission and Towers,” to which it also applies the intraMSA factor. Similarly, the transmission links to the towers are analogous to the feeder trunks that connect an ILEC switch to remote terminals. ILECs can build networks with

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<sup>161</sup> *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, First Report and Order, 11 FCC Rcd 15499, 15510 (¶¶ 14-15) (1996). The FCC later changed the language of this rule to delete the word “local”, but the MSA boundaries are still used to distinguish traffic subject to access from the traffic subject to reciprocal compensation.

substantial feeder plant, and this feeder plant would all be classified as loop plant, irrespective of the amount of intraMSA usage. Yet WiCAC proposes to apply the intra MSA factor to trunks connecting the wireless MSC to towers, and to reduce the “loop” allocation by the amount of non-local usage.

For ILECs, the Commission takes the ILEC networks as they find them. “Loops” are defined as the link between the switch and the end user.<sup>162</sup> There is no adjustment for “long” loops or “short” loops. It would be wholly discriminatory to adopt a different approach solely for CETC networks. Thus, in addition to being unworkable, overly regulatory and unwieldy, the WiCAC proposal is highly discriminatory and lacks any rational basis for its discriminatory features.

**E. There is no Need to Require CETCs to Submit Costs by Disaggregation Zone.**

The NPRM suggests that CETCs be required to track costs by disaggregation zone.<sup>163</sup> This is unnecessary. The purpose of disaggregation zones is to reflect the fact that costs vary in different parts of the study area, and thus, when CETCs are being paid the ILEC’s level of per line support, per line support should vary across the study area to reflect differences in underlying cost.<sup>164</sup> For ICLS, LSS and HCLS, ILEC support is

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<sup>162</sup> 47 C.F.R. Part 36, Appendix – Glossary (defining “loop” as “A pair of wires, *or its equivalent*, between a customer’s station and the central office from which the station is served.”) (emphasis added).

<sup>163</sup> *Equal Support NPRM*, 23 FCC Rcd at 1474-75 ¶ 16.

<sup>164</sup> *RTF Order*, 16 FCC Rcd at 11302 ¶ 145 (“Because support is averaged across all lines served by a carrier within its study area under the existing mechanism, the per-line support available throughout the study area is the same even though the costs throughout the study area may vary widely. As a result, artificial barriers to competitive entry in the highest-cost areas and artificial entry incentives in relatively low-cost portions of a rural carrier’s study area are created. For example, support would be available to a competitor that serves only the low-cost urban lines, regardless of whether the support exceeds the cost of any of the lines. We conclude

determined based on aggregated study area costs, not the disaggregated costs by zone. Thus, in the absence of disaggregation, under the existing equal support rule, the CETC is paid the ILEC support per line averaged across the entire ILEC study area, irrespective of whether lines are in low cost or high cost areas. As the Commission observed, this has created both artificial barriers to competitive entry in high cost areas, and artificial incentives to competitive entry in low cost areas.

In an “own costs” system, however, CETCs would not be paid based on the ILEC’s effective per line support. Instead, because CETCs would be required to report their costs for the study area, and those costs would be used as the basis for calculating CETC support, they would already automatically receive less support if they served only the low cost portions of a study area, because their reported loop costs (for HCLS and ICLS) would be lower. On the other hand, if they serve the entire study area, including the higher cost areas, then they receive greater support. Thus, the disaggregation zones would be irrelevant to calculating CETC support. Accordingly, CETC should not be required to report costs below the study area level.

**F. CETC “Own Costs” Support Should not be Unilaterally Capped.**

In another example of putting its “thumb on the scales,” the *Equal Support NPRM* proposes to cap CETC support under the “own costs” mechanism at the ILEC’s per line support level.<sup>165</sup> While this might seem reasonable at first blush, it is not, and further illustrates why an “own costs” mechanism for CETC support should be rejected. In the

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therefore that, as a general matter, support should be disaggregated and targeted below the study area level so that support will be distributed in a manner that ensures that the per-line level of support is more closely associated with the cost of providing service.”).

<sup>165</sup> *Equal Support NPRM*, 23 FCC Rcd at 1478 ¶ 25.



first instance, if a significant purpose of moving to “own costs” support is to incent CETCs to serve high cost or even unserved areas, the proposed cap would have the opposite effect. The only costs that the ILEC reports are study area average costs, not disaggregated costs. Thus, such a cap would understate the costs of a CETC serving the high cost portions of the study area and create an artificial barrier to entry in the high cost portions of the ILEC study area.<sup>166</sup> Unlike disaggregation under the equal support rule, however, this proposed cap does not give the CETC the opportunity to have a higher per line support in the high cost areas than in the low cost areas.

Indeed, the cap proposal appears to assume that the ILEC actually has extended its network everywhere in the study area and is providing high quality services everywhere. That is not necessarily the case. As CETCs such as GCI deploy new technologies, particularly more robust wireless services in rural areas, GCI may begin to serve customers that are not served by the ILEC’s wireline network because a customer may be able to be served by GCI without incurring the line extension charges that they would have to pay the ILEC to receive service. Alternatively, GCI may deliver a much higher quality of service than the ILEC, particularly where the ILEC may be using its own wireless local loop service. This would be the case, for example, in the communities at issue in the RCA’s current investigation of ACS’s prolonged and repeated service outages.<sup>167</sup> Capping CETC support at the ILEC average per line support levels within the study area would penalize the CETC for providing such service improvements.

Alternatively, if the Commission is going to adopt a cap, it should be a non-discriminatory, bilateral cap. In other words, the support of both the ILEC and the CETC

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<sup>166</sup> See *supra* n.164.

<sup>167</sup> See *supra* Part I.

should be capped at the lower effective per line support for both carriers. There is no more reason for the ILEC to receive support for costs above the CETC's than for the CETC to receive support for costs above the ILEC's. To the extent the Commission has a concern that ETCs (whether CETCs or ILECs) have an incentive to inflate costs under "own costs" universal service support,<sup>168</sup> that incentive exists for both ILECs and CETCs. Addressing that incentive only for CETCs is both unreasonably discriminatory and bad policy for eliminating waste, fraud and abuse. Indeed, because ILEC support constitutes 75 % of all high cost support, the Commission should not ignore incentives for ILECs to inflate costs across that vast majority of high cost support.

#### **PART C – COMMENTS FOCUSED ON THE *REVERSE AUCTION NPRM***

##### **VI. Any Reverse Auction Must Be Clearly Defined and Must not Foreclose or Impede Competition.**

The *Reverse Auction NPRM* maintains that "reverse auctions could provide a technologically and competitively neutral means of controlling fund growth and ensuring a move to most efficient technology over time."<sup>169</sup> GCI agrees in theory, but the *Reverse Auction NPRM* wrongly treats a reverse auction as a replacement for the competitive marketplace that will heal many of the ills of the current high-cost support program.<sup>170</sup> Even a well-defined and well-implemented reverse auction will only provide a partial cure for the universal service high-cost fund.

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<sup>168</sup> *Equal Support NPRM*, 23 FCC Rcd at 1478 ¶ 25 ("Adopting a ceiling for competitive ETCs at the level of incumbent LEC support could avoid rewarding competitive ETCs for being inefficient and reduce incentives for competitive ETCs to inflate their costs.").

<sup>169</sup> *Reverse Auction NPRM*, 23 FCC Rcd at 1498 ¶ 4; *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Public Notice, WC Docket No. 05-337 and CC Docket No. 96-45 at 2 (¶ 4) (rel. May 1, 2007).

<sup>170</sup> See *GCI Reverse Auction Comments*.

**A. The Commission Must Answer Core Questions in Advance of Any Auction.**

As discussed above, attempting universal service reform without first settling certain threshold, definitional questions is all but useless. This is especially true for any reform that institutes a reverse auction. Potential bidders must know, before the auction, what services they are required to provide, at what cost, over what area, and under what terms and conditions. The *Reverse Auction NPRM* at least begins the discussion of some of these issues, *e.g.*, tentatively concluding to require broadband service at a “reasonable” price and asking whether ETCs are required to provide wireline and wireless service, but does not go nearly far enough in defining these fundamental issues.

**B. Limiting Support to One Auction Winner Will Harm Rural America.**

Although the auction process is by nature competitive, an auction that produces a single “winner” is not a suitable substitute for real marketplace competition, particularly in a fast-changing, technologically-driven marketplace. Thus, the Commission’s tentative conclusion that universal service auctions should award high-cost support to only a single winner is misguided.<sup>171</sup>

A reverse auction that allows only a single ETC – or even that limits the winners to one wireless and one wireline ETC<sup>172</sup> – will wring competition out of markets where it might have developed; create government-sanctioned, but still inefficient, monopolization; lock technological developments out of the market; and ultimately prevent the natural decrease in high-cost support that competition will engender. As

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<sup>171</sup> *Reverse Auction NPRM*, 23 FCC Rcd at 1501 ¶ 14.

<sup>172</sup> See *High Cost Universal Service Support; Federal-State Joint Board on Universal Service*, Verizon Ex Parte and attached Letter to Commissioners Tate and Baum, WC Docket No. 05-337 and CC Docket No. 96-45, at 7-8 (filed Feb. 9, 2007).

Chairman Martin has previously acknowledged, “[i]f the Commission implemented a reverse auction and limited the number of lines, but *allowed multiple providers to receive support, it could serve to stem growth [of the fund]*.”<sup>173</sup> This is especially true because technology is rapidly changing. Had single winner auctions existed five years ago, GCI would not now be able to obtain support needed to deploy its rural wireless service to remote villages in Alaska. Locking in single providers ignores the significant potential for advances in delivering cost-effective universal services to rural areas. This is no less true if the auction allows one wireless ETC and one wireline ETC auction winner, as Verizon has proposed.<sup>174</sup> Because wireless and wireline ETCs provide predominantly complementary, rather than substitute, service, Verizon’s proposal will not provide real competition and thus flies in the face of basic economics. Moreover, as these services converge and in the future become true substitutes, the need for the artificial distinction disappears. Allowing multiple ETCs to compete both in auction-bidding and in post-auction provision of services, regardless of technology, is the best way to encourage innovation for rural consumers.

Further, if auction terms are fairly long, a single winner auction will install a monopoly provider, with no incentive to respond to technological changes and potential competition during the license term. As such, GCI believes that five years between auctions, as the Commission suggests,<sup>175</sup> is too long to foster the type of competition that will ultimately drive down the costs of providing universal service.

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<sup>173</sup> Responses to Chairman Markey’s April 2, 2007 Letter at 3 (emphasis added).

<sup>174</sup> See *Reverse Auction NPRM*, 23 FCC Rcd at 1498 ¶ 6.

<sup>175</sup> *Reverse Auction NPRM*, 23 FCC Rcd at 1508-09 ¶ 35.

GCI's rural network will deploy wireless technologies that were not available a few years ago. If the Commission had employed a single-winner auction five years ago, GCI would have been locked out of the market for the term of the auctioned license, even though technological changes would have otherwise allowed competition during the interim. Accordingly, as GCI has explained previously,<sup>176</sup> the Commission should use an auction not to decide *which provider* will serve any particular high-cost area, but instead to determine the *amount of subsidy* necessary for an efficient and capable provider to serve the defined market and then allow any ETC to receive per line support for that market. As Dennis Weller has explained, “[i]f we wish to design a universal service program that is compatible with competition, it hardly seems reasonable to begin with a model that assumes a single universal service provider.”<sup>177</sup> Instead, allowing multiple bidders to win an auction can harness the benefits of “competition for the market” – in which carriers compete for the right to serve as one of a limited number of supported carriers – without foreclosing “competition in the market” – in which several carriers accept universal service obligations and compete to acquire subscribers and the associated support payments.<sup>178</sup> Under Weller’s proposal, bidders within a certain range are accepted and allowed to compete for universal support for a given area, while bidders

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<sup>176</sup> See generally *GCI Reverse Auction Comments*.

<sup>177</sup> Dennis Weller, *Auctions for Universal Service Obligations*, 23 Telecommunications Policy 645, 654 (1999) (“Weller”). But see *Federal-State Joint Board on Universal Service; High Cost Universal Service Support*, Verizon Ex Parte Letter, Appendix, WC Docket No. 05-337 and CC Docket No. 96-45 (filed Feb. 9, 2007), in which Dennis Weller, as Chief Economist for Verizon, advocated for a “one-winner” auction model.

<sup>178</sup> *Weller* at 654.

outside a certain range are excluded for three years to provide incentive to bid “for the market.”<sup>179</sup>

A reverse auction that allows multiple ETC competitors also avoids the legal infirmities of mandating a sole supported ETC, which as discussed above contravenes the Act’s express language and structure.<sup>180</sup>

**C. The Consumers and the Market Should Decide Whether a Service Area Can Support More than One Carrier.**

That a single provider will most efficiently provide universal service in hard-to-serve rural areas is contrary to both the rationale of the 1996 Telecommunication Act and the worldwide economic experience during the twentieth century. The 1996 Act expressly rejected the notion that telecommunications would be best provided by local monopolies, regulated to serve the public interest, and instead embraced competitive markets. The world as a whole during the twentieth century saw the same thing: in no setting has the selection of a single provider by the government (such as in the Soviet Union and Cold War Eastern Europe) proven to be a more effective means of economic organization than a competitive market. While there may be some areas of the market that will support only one ETC (or just one wireless and one wireline ETC), the market itself – not regulators under the guise of a reverse auction – will best make that determination. Any reverse auction should be structured to let “the ‘invisible hand’ of self-correcting market mechanisms, not regulatory fiat, determine[] the number and the identity of firms that thrive in the marketplace.”<sup>181</sup>

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<sup>179</sup> *Id.* at 667-68.

<sup>180</sup> *See supra* Part III.B.

<sup>181</sup> Sappington at 19.

**D. The Auction Should be Open to ETC Applicants, as Well as ETCs.**

Reverse auctions should not limit participation to current ETCs. The state-run ETC approval process can at times be lengthy. It would frustrate the competitive purposes of an auction to prevent otherwise qualified bidders from participating because a state commission may not have acted quickly enough to approve an ETC application. Moreover, to the extent that the Commission may be worried about issues of an ETC applicant's character or financial qualifications, those can and should be addressed in the bid qualification requirements. Accordingly, the Commission should reverse its tentative conclusion that a bidder must hold an ETC designation prior to participating in the auction.<sup>182</sup>

**E. ILECs Must Not Receive Special Protections.**

No auction mechanism can be efficient and fair unless it applies evenly to all qualified providers. In this context, it must be expressly acknowledged and permitted that the amount of support may be less than what some providers bid. If the incumbent loses the auction, it should not be entitled to extra support, unless that support is also available to other bidders. Similarly, an incumbent should not be given any preference in bidding. Finally, incumbents must also be capable of losing any auction. In other words, if any provider may be excluded as a result of an auction, incumbents must also be capable of being excluded. Otherwise, the incumbents will have an overwhelming advantage in bidding, and have no incentive to bid low. Other carriers' bids would also be skewed by their efforts to offset these biases. As a result, incumbent preferences

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<sup>182</sup> *Reverse Auction NPRM*, 23 FCC Rcd at 1500-01 ¶ 12.

would necessarily undermine the chief benefits of an auction by distorting, rather than revealing, information about carriers' costs and the efficient level of subsidy.

## CONCLUSION

The Commission should not turn its back on either the ideals or the intended beneficiaries of universal service by abandoning competition in the name of reform. Instead, the Commission should consider reforms that preserve existing support for chronically underserved tribal lands, reduce the size of the fund by limiting all ETCs to one support payment per residential/single-line business account, and include long-awaited numbers-based contribution reform. Moreover, as the Commission considers long-term reform, it must define the specific objectives that it seeks to achieve, including key statutory terms such as “affordable,” “reasonably comparable” and “sufficient.” Most importantly, it must keep in mind that in rural as well as in urban America, competition is the best driver of continued innovation and efficiency. Locking rural America into a single universal service provider condemns rural America to second-class communications services.

Respectfully submitted,

/s/

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April 17, 2008